

# FINANCIAL SERVICES AND GENERAL GOVERNMENT APPROPRIATIONS FOR 2014

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## HEARINGS BEFORE A SUBCOMMITTEE OF THE COMMITTEE ON APPROPRIATIONS HOUSE OF REPRESENTATIVES ONE HUNDRED THIRTEENTH CONGRESS FIRST SESSION

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### **PART 6**

	<b>Page</b>
<b>U.S. Securities and Exchange Commission .....</b>	<b>1</b>
<b>U.S. Securities and Exchange Commission .....</b>	<b>45</b>
<b>General Services Administration .....</b>	<b>127</b>
<b>Small Business Administration .....</b>	<b>193</b>



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# **FINANCIAL SERVICES AND GENERAL GOVERNMENT APPROPRIATIONS FOR 2014**

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TUESDAY, MARCH 12, 2013.

## **U.S. SECURITIES AND EXCHANGE COMMISSION**

### **WITNESS**

#### **CARL W. HOECKER, INSPECTOR GENERAL**

Mr. CRENSHAW. The meeting will come to order.

Today we are going to hear from Inspector General Carl Hoecker. He and I have known each other from my time as Chair of the Leg Branch Subcommittee when he was the Inspector General for the U.S. Capitol Police. So I am pleased to welcome him back and hope that we will continue our great working relationship.

Inspector Hoecker was just appointed about 1 month ago in this new position. So we appreciate you coming up so quickly to testify, having just started your new position. We are anxious to hear what you have planned for your office.

This subcommittee has distinct jurisdiction over a diverse group of agencies, and many of those have a profound impact on American lives. The SEC is one of those agencies. It has the unique task of protecting investors, maintaining fair and efficient markets, and encouraging capital formation. This is a tall order. Having an effective Inspector General conducting oversight over an agency as large and as important as the SEC is obviously very critical.

Since 2001, Congress has provided the SEC with additional regulatory tools, and we have more than doubled the commission's annual appropriations. And yet the agency missed the Madoff and the Stanford Ponzi schemes; the agency has made expensive mistakes with regard to their leasing authority; and they have made wasteful decisions with regard to their procurement and contracting.

And so, Mr. Inspector General, you are our eyes and ears. You are the watchdog of the taxpayers. So it is my expectation that your office is actively looking for improvements and efficiencies within the SEC to make sure that our taxpayers' dollars are being spent efficiently. So we look forward to hearing your testimony, and look forward to hearing the answers to our questions.

Before I ask you to proceed, I would like to call on Ranking Member Serrano for any opening statement he might have.

Mr. SERRANO. Thank you, Mr. Chairman.

And I would also like to welcome Mr. Hoecker, the new inspector general for the Securities and Exchange Commission to testify before the subcommittee.

I believe this may be your first time testifying before Congress in your new position. So we promise to be gentle and sweet and charming.

In recent years, the SEC has received numerous new responsibilities and has received an increased budget from this subcommittee to help deal with those responsibilities. Your office has the important job of making sure that those new resources are being used effectively and efficiently. And that the SEC is properly performing its job of protecting investors and consumers. I know, in the past, the OIG's office has been very responsive to questions from this subcommittee on these sorts of issues. And as we move into the fiscal year 2014 budget cycle, I hope we can continue this productive dialogue.

Unfortunately, we cannot go through these hearings without discussing sequestration, which, according to the CBO, will reduce our gross domestic product by six-tenths of a percentage point in this year alone. Moreover, the sequester is going to severely impact the ability of agencies, like the SEC, to perform the basic functions that the American people expect of them. I am very concerned that as a result of sequestration, we are reducing resources for the SEC at the very time we are asking them to take on more work through the continued implementation of Dodd-Frank.

Sequestration is being compounded by the proposed continuing resolution for fiscal year 2013, which it appears will not provide additional funding to the SEC. We need to make sure the SEC has sufficient resources to guard our financial markets against fraud and abuse. I am interested in learning more about what your office will be doing to monitor the effects on the SEC and how you will analyze whether your agency has sufficient resources to do the job we have given them.

Sequestration issues are also likely to affect the operation of the OIG's office as well. Although you have only been in your new position for a short time, I hope you will be able to detail for us the impact of the sequester on your increasingly large mission as well. So we welcome you and we look forward to your testimony.

Thank you, Mr. Chairman.

Mr. CRENSHAW. Thank you.

So, Mr. Hoecker, we would now like to call on you to make an opening statement. If you could limit that to 5 minutes or less, it will give us more time to ask you questions, and we will accept your written statement for the record. Please proceed.

Mr. HOECKER. Thank you.

Good afternoon, Chairman Crenshaw, Ranking Member Serrano, members of the subcommittee. Today it is my privilege to introduce myself as the newly appointed inspector general for the Securities and Exchange Commission.

In my testimony, I am representing the Office of Inspector General, and the views expressed are my own and my office's and do not necessarily reflect the views of the Commission or any Commissioner. Despite the constrained fiscal environment facing our Nation, we feel that the aggregate budget request for the operations of OIG for fiscal year 2014, which is \$7.8 million, is justified as we continue to focus on improving agency programs through audits of



programs and operations, emboldening staff and integrity, agency integrity by investigating allegations of misconduct.

As the SEC strives to ensure confidence in our capital markets, we continue working with the Commission to assist it in its mission to protect investors, maintain fair, orderly, and efficient markets, and facilitate capital formation. I envision that with my experience in investigations and forensic accounting, I will effectively be the eyes and ears of Congress and be a steadfast independent advisor for the commission.

I would like to begin my remarks by briefly discussing the role of the OIG and its oversight efforts for the next few years. The OIG is an independent office within the SEC that conducts audits of programs and operations and investigations into misconduct by agency staff, and contractors. Our office, in accordance with the IG Act of 1978, as amended, does not set policy for the SEC nor make substantive determinations regarding the Commission's program functions or budgetary process; rather, our mission is to promote integrity, efficiency, and effectiveness of programs and operations and to report our findings and recommendations to the agency and to Congress. Since my appointment as IG for the SEC last month, the OIG investigative and audit units have continued vigorous oversight over the SEC.

The Office of Audits includes six auditors who report to the Assistant IG for Audits. During fiscal year 2012, the OIG issued eight audit reports involving matters critical to the SEC programs, including cost-benefit analyses conducted for six rulemakings pursuant to Dodd-Frank, the SEC's continuity of operations, and record management practices. The reports contained 102 recommendations with which the agency fully concurred. We also saw closures of 155 recommendations from OIG reports issued during and prior to fiscal year 2012. In this current fiscal year, our audit function has issued one audit report, issued five draft reports to SEC management and continues to work on five additional assignments.

The SEC Office of Investigations includes six investigators who report to the Assistant IG for Investigations. Notwithstanding the small size of the investigative staff, the Office of Investigations has conducted numerous investigations and inquiries involving violations of statutes, rules, regulations, and other misconduct. In fiscal year 2012, OIG received 535 complaints, and opened 10 investigations, and 45 preliminary inquiries based on those complaints. In the same time period, the OIG concluded 15 investigations and 75 preliminary inquiries, resulting in 5 referrals to the Department of Justice and 11 referrals to agency management for consideration of administrative action. To date, in fiscal year 2013, the OIG has received approximately 220 complaints, has opened 7 investigations, 8 preliminary inquiries, and has concluded three investigations and 20 preliminary inquiries.

I believe that the SEC's mission of protecting investors; maintaining fair, orderly and efficient markets; and facilitating capital formations is more important as ever. As our Nation's securities exchanges mature into global for-profit competitors, there is even greater need for sound market regulation. At the same time, the SEC has responsibility to utilize government funds in an efficient and effective manner. And, the OIG intends to remain vigilant to

ensure that scarce government resources are utilized wisely and cost effectively, and that instances of fraud, waste, and abuse are eliminated. I appreciate the interest of the subcommittee in the SEC and my office. I believe that the subcommittee's and the Congress' continued involvement with the SEC is helpful to strengthen the accountability and effectiveness of the commission. And this concludes my verbal statement, and I am happy to answer any questions you may have. Thank you.

[The information follows:]

**Written Testimony of Carl W. Hoecker  
Inspector General of the  
Securities and Exchange Commission**



**Before the Subcommittee on Financial Services and  
General Government, Committee on Appropriations,  
U.S. House of Representatives**

**Tuesday, March 12, 2013**

### **Introduction**

Mister Chairman and Members of the Subcommittee, today it is my privilege to introduce myself as the newly appointed Inspector General of the U.S. Securities and Exchange Commission (“SEC”). In my testimony, I am representing the Office of Inspector General (“OIG”). The views expressed are those of myself and my office, and do not necessarily reflect the views of the Commission or any Commissioners.

Despite the constrained fiscal environment facing our nation, we feel our aggregate budget request for the operations of the OIG for Fiscal Year 2014 (\$7.848 million) is justified as we continue to focus on improving agency programs and operations through audits, evaluations, and reviews, while emboldening staff and agency integrity by investigating allegations of employee and contractor misconduct. As the SEC strives to ensure confidence in our capital markets, we continue working with the Commission to assist in its mission to protect investors, maintain fair, orderly, and efficient markets, and facilitate capital formation. I envision that with my experience in investigations and forensic accounting, I will effectively be the “eyes and ears” for Congress and be a steadfast and independent advisor for the Commission.

### **Role of the OIG**

I would like to begin my remarks by briefly discussing the role of my office and the oversight efforts we anticipate for the next few years. The OIG is an independent office within the SEC that conducts audits of programs and operations of the Commission and investigations into allegations of misconduct by agency staff and contractors. Our office, in accordance with the Inspector General Act of 1978, as amended, does not set policy for the SEC nor make substantive determinations regarding the Commission’s

program functions or budgetary process. Rather, our mission is to promote the integrity, efficiency, and effectiveness of the programs and operations of the SEC, and to report our findings and recommendations to the agency and Congress. Since my appointment as Inspector General of the SEC last month, the OIG's investigative and audit units have continued vigorous oversight of the SEC.

### **SEC OIG Audits, Including Audits of Rulemaking Cost-Benefit Analyses**

The Office of Inspector General's Office of Audits is comprised of six auditors who report to the Assistant Inspector General for Audits. During Fiscal Year 2012, the OIG issued eight audit and evaluation reports involving matters critical to SEC programs and operations, including the cost-benefit analyses conducted for six rulemakings made pursuant to the Dodd-Frank Act (as discussed further below), the SEC's continuity of operations program, and records management practices. The reports issued contained 102 recommendations with which the agency fully concurred. We also saw the closure of 155 recommendations, from OIG reports issued during and prior to Fiscal Year 2012.

On June 13, 2011, the OIG released an audit report entitled, "Report of Review of Economic Analyses Performed by the Securities and Exchange Commission in Connection with Dodd-Frank Act Rulemakings. In that report, the OIG reviewed the cost-benefit analyses performed by the SEC in connection with six specific rulemaking initiatives pursuant to the Dodd-Frank Act. The OIG concluded that the SEC had conducted a systematic cost-benefit analysis for each of the six rules, but found that the level of involvement of the Division of Risk, Strategy and Financial Innovation (RiskFin) varied considerably from rulemaking to rulemaking.

On January 27, 2012, the OIG issued an additional report entitled, “Follow-up Review of Cost-Benefit Analyses in Selected Dodd-Frank Act Rulemakings.” In the second review, the OIG’s objectives were to assess whether the SEC was performing cost-benefit analyses for rulemaking initiatives that were statutorily required under the Dodd-Frank Act in a reliable manner, and to determine whether areas existed where rigorous cost-benefit analyses were not performed and where best practices could be identified to enhance the overall methodology used to perform cost-benefit analyses. In the follow-up report issued on January 27, 2012, the OIG found that although the SEC is not subject to a specific statutory requirement to conduct cost-benefit analyses for its rulemakings, it is subject to various statutory requirements to consider factors such as the proposed rule’s effects on competition and the needs of small entities.

The second report also noted that the previous SEC Chairmen had committed to Congress that the SEC would conduct cost-benefit analyses in connection with its rulemaking activities, and that the agency had made a practice of performing such analyses in its rulemakings. Furthermore, the OIG found that to the extent that the SEC performs cost-benefit analyses only for discretionary rulemaking activities without a pre-statute baseline, the SEC may not be providing a full picture of whether the benefits of a regulatory action are likely to justify its costs and which regulatory alternatives would be the most cost-effective. We also noted that some SEC Dodd-Frank Act rulemakings lacked clear, explicit explanations of the justification for regulatory action. The report found that a more focused discussion of market failure in cost-benefit analyses would identify the rationale for regulation more clearly to Congress, the general public, and the SEC itself. Finally, the review found that although some of the SEC’s Dodd-Frank Act

rulemakings may result in significant costs or benefits to the Commission itself, internal costs and benefits were rarely addressed in the cost-benefit analyses.

Based on the results of the review, the report made several recommendations for improvements to the SEC's practices. SEC management concurred with all but one of the report's recommendations; however, they took actions sufficient for OIG to close all the recommendations in the report.

### **SEC OIG Investigations**

The SEC OIG's Office of Investigations is comprised of six investigators who report to the Assistant Inspector General for Investigations. Notwithstanding the small size of the investigative staff, the Office of Investigations has conducted numerous investigations and inquiries into alleged violations of statutes, rules and regulations, and other misconduct by Commission staff and contractors. In Fiscal Year 2012, the OIG received approximately 535 complaints, and opened 10 investigations and 42 preliminary inquiries based upon those complaints. In this same time period, the OIG concluded 15 investigations and 75 preliminary inquiries, resulting in 5 referrals to the Department of Justice and 11 referrals to agency management for consideration of administrative action. To date in Fiscal Year 2013, the OIG has received approximately 220 complaints, has opened 7 investigations and 8 preliminary inquiries, and has concluded 3 investigations and 20 preliminary inquiries.

The investigative reports issued by the OIG during FY 2012 and FY 2013 have addressed a wide variety of allegations, including alleged procurement violations and conflicts of interest, misuse of government resources, security violations, fraud and falsification of benefits documents, unauthorized disclosure of nonpublic information,

and prohibited personnel practices. Most significantly, in August 2012, the OIG issued a report of investigation concerning various information technology security violations and mismanagement within a lab in the SEC's Division of Trading and Markets.

Specifically, the OIG's investigation found that since 2006, lab staff had spent over \$1 million dollars on computer equipment and software with little oversight or planning, and that a significant portion of the equipment and software purchased was unnecessary or never used. We also found that some of the lab's equipment was taken home by lab employees and used primarily for personal purposes, and that some equipment was purchased based on misrepresentations made by lab staff in contacting documents. The OIG investigation further found that lab staff violated SEC information technology security policies and took laptops without proper encryption and virus protections on inspections. SEC management promptly began to take action to address the OIG's findings. We are currently completing a follow-up investigation to review management's response to the OIG's report and to determine whether any sensitive information was compromised as a result of the identified security violations.

### **Conclusion**

I believe that the SEC's mission of protecting of investors, maintaining fair, orderly, and efficient markets, and facilitating capital formation is more important than ever. As our nation's securities exchanges mature into global, for-profit competitors, there is even greater need for sound market regulation. At the same time, the SEC has a responsibility to utilize government funds in an efficient and effective manner. The OIG intends to remain vigilant to ensure that scarce government resources are utilized wisely and cost-effectively, and that instances of waste and abuse are eliminated.



I appreciate the interest of the Subcommittee in the SEC and my Office. I believe that the Subcommittee's and Congress's continued involvement with the SEC is helpful to strengthen the accountability and effectiveness of the Commission. Thank you.

**Carl W. Hoecker, CPA/CFF, CFE**  
**Inspector General, U.S. Securities and Exchange Commission**

Carl W. Hoecker is an accomplished professional with more than 30 years of experience in federal law enforcement and accounting. He has supervised and conducted specialized financial investigations, forensic audits and reviews, and led fraud prevention and business process improvement efforts in the U.S. military and federal civilian agencies.

On Feb. 11, 2013, Mr. Hoecker was appointed as the Inspector General (IG) of the U.S. Securities and Exchange Commission (SEC). As IG, Mr. Hoecker leads a team of auditors, investigators, and administrative staff to fulfill the mission of the SEC Office of Inspector General (OIG) to promote the integrity, efficiency, and effectiveness of the SEC's programs and operations.

In 2006, Mr. Hoecker was appointed the first IG for the U.S. Capitol Police. As a result of his leadership, the Capitol Police OIG is relied upon as a trusted, steadfast advisor to the Chief of Police, Capitol Police Board, and Congress. During Mr. Hoecker's tenure, the Capitol Police OIG conducted extremely sensitive investigations and audits, identified weaknesses, and made recommendations to improve internal controls and ensure government funds were spent wisely.

Mr. Hoecker began his career with the U.S. Army in 1976 as a military policeman, later becoming a special agent and warrant officer for the Army Criminal Investigations Command. During his last assignment in the Army, he was a member of an investigative unit charged with investigating procurement fraud and fraud prevention measures within the classified community. In 1992, he joined the IG community as a criminal investigator, later becoming Deputy Assistant Inspector General for Investigations at the U.S. Treasury OIG.

Mr. Hoecker graduated from Governor's State University with a Bachelor of Arts degree in Business Administration and has a Master's degree in Systems Management from the University of Southern California. He is a Certified Public Accountant (CPA), Certified Fraud Examiner, Certified Government Financial Manager, and is Certified in Financial Forensics. Mr. Hoecker serves as the chairman of the Investigations Committee for the Council of Inspectors General for Integrity and Efficiency and is a member of the Virginia Society of Certified Public Accountants and the American Institute of CPAs.

Mr. CRENSHAW. Thank you, Mr. Hoecker.

Let me start by asking you a little bit about the sequester and the impact that it has. I think everybody knows that we have been struggling here in Congress along with the executive branch to try to get a handle on some of our debt and some of the deficit. We raised taxes back at the first of this year. We are working on tax reform. We are working on entitlement reform. We have still got a ways to go. One of the good things I think we would all agree on this subcommittee and our full Appropriations Committee is, from 2010 to 2012, we actually reduced discretionary spending. We made some tough choices, and spending went down \$95 billion.

But here we are in a situation where we have a continuing resolution. I think we all agree on this subcommittee, that is not the best way to run the railroad. It kind of throws out all the work that we put in last year. And we still haven't resolved some of the issues related to the Budget Control Act, finding that extra \$1.2 trillion. So here we are with a sequester.

Once again, I think most would agree that if you have to cut spending, and not everybody agrees that you do, but I think regardless of how you feel about it, we would all say across-the-board cuts are really not the best way to do it. They ought to be targeted. They ought to be smart. We ought to look at priorities: Things that are being wasted, we ought to cut; things that are being done well, we ought to increase.

So here we are, and we still don't have a budget yet from the executive branch. But we appreciate you being here to talk about some of the issues that are before us.

So, in that regard, I would love to know what—even though you are brand new, and I am sure you are working night and day—what would you say the impact of the sequester has been so far, just on your little corner of the world, as Inspector General? And then maybe if you can make a comment on how you think it has impacted the full SEC. Equally as important, I would love to know what you think about these cuts, as it relates to your part of the world, to the agency. When you have to go through these kind of cuts that are going to amount to about 5 percent, about 8 percent to the Defense Department, does that make you try to conduct your business even more efficiently? Because you have to live with that; we don't know how long it is going to be. Please comment on the impact it might have had on you already, and what do you think the impact will be as you move forward?

Mr. HOECKER. Yes, sir. Well, one of the first things I found when I took over the job a month ago is that I needed to get a handle on how sequestration will affect my office. And good or bad, we found that for the OIG, it will not have furloughs this fiscal year, due to the fact that we are down—we need to hire eight people. So we had some folks leave and things like that. So, from that perspective, there is sufficient salary lag, if you will, that it won't affect my office.

The second thing I wanted to find out, at least in terms of if there is going to be any shut down within the SEC or layoffs, furloughs, was to ask the CFO. So I had a visit with the CFO either my second or third week, and he assured me that the sequestration will result in no furloughs or reductions in force at the SEC.

In terms of any impact on the program and delivering the regulation, et cetera, sir, I don't have any body of work to support that, and I will have to blame that on my newness in terms of reduction of budget and if there is going to be any negative effect on the program itself, sir.

Mr. CRENSHAW. Do you think overall it motivates you and your agency to just try to be more efficient? I would think that is the case.

Mr. HOECKER. Well, what I always try to do, sir, if Congress sees fit to give me a certain amount of money. And I need to make it work.

Mr. CRENSHAW. Got you.

Mr. HOECKER. Need to deliver the mission.

Mr. CRENSHAW. I got you.

One other quick question. The one concern I hear about the rule-making process, and again this is more SEC, but as you look at how they make rules, the two big concerns, it seems to me, are, number one, how they use the cost-benefit analysis in their rule-making. Over time I have heard that that is lacking in some cases. And the other concern that people have about rulemaking that the Commission does, is that they undertake rulemaking not so much that is required by, say, Dodd-Frank or some other statute, but they have taken up nonstatutorily required rulemakings. I think the prior Chairman talked about rules relating to money market funds, and the new Chairman is said to be interested in campaign contributions, things that aren't necessarily a priority from the standpoint of the statute. I just wondered if you had a chance to look at some of these concerns—particularly the cost-benefit analysis. Can you comment on that? Have you taken a look at these?

Mr. HOECKER. Yes, sir. I have taken a look at the work that we have done. And about—we have issued two reports on rulemakings, and we are currently underway with another phase, two-phased approach.

What this current two-phased approach that is ongoing in audit is that the former chair committed to, there is a guidance memo on including cost-benefit analysis with rulemaking. And she had committed that the agency, the commission would implement that.

So we are doing an audit to the extent to find out where they documented that, how it looks and what kind of cost-benefit analysis they have looked at. There are other certain objectives that I can share with you. But that is kind of the big picture that we are looking at right now.

Mr. CRENSHAW. Thank you very much.

Mr. HOECKER. And that we have committed to issue that final report at the end of April. So I will go ahead on record saying end of April. But I will also go on record to say that I want to make sure I am comfortable with it before I release it. So if it is a week late, I will take the wrath, but I want to make sure I am comfortable with the product.

Mr. CRENSHAW. Great. Thank you very much.

Mr. Serrano.

Mr. SERRANO. Thank you, Mr. Chairman.

We know, sir, that your role as IG has certain responsibilities and areas that you cover. But, of course, you recommend to the SEC certain things.

And in view of the fact that the SEC has not received what the President has asked for in the last couple of years, that the Senate bill introduced yesterday does not provide any funding above 2012, and sequestration, how confident are you that the SEC can tackle the many challenges that it faces? And, more importantly, in your case, can they fully implement your recommendations?

Mr. HOECKER. Well, I would say that they are going to have to make it work, sir. I have only been there for 4 weeks. And I don't have a body of knowledge to analyze the impact of keeping it at the 2012 level.

But I would just say they will make it work. The folks that I have met are very committed to the mission. If they requested a certain amount, that is what they felt they needed. I just can't answer the delta and what the effect of the delta would be, sir.

Mr. SERRANO. Now, we know it is somewhat if not very unfair to ask you after 4 weeks to have a full picture, and you have made that clear, and we understand that.

But in those 4 weeks, are there any areas you have seen where the budget of the SEC would be hit hard and would impair them from moving forward with some things that you may know at this point early on? And realize it is not a full analysis, but just something.

Mr. HOECKER. I haven't looked at the budget in detail, sir, so I don't know if I could give you an answer on that.

Mr. SERRANO. All right. And on your particular—the work you have to do, you say you will make it work.

Mr. HOECKER. Yes, sir.

Mr. SERRANO. But certainly making it work and hoping it was different are two different things. We are here as appropriators, not all the time to suggest cutting the budget. I know that sounds strange. We also want to invest every so often.

Mr. HOECKER. Yes, sir.

Mr. SERRANO. So you shouldn't shy away from telling us "I would like to see this happen in my particular agency." And I just want you to keep that in mind.

But after 4 weeks, I guess you can't tell us, other than you will make it work what other, how the budget will hurt you in your ability to make your recommendations?

Mr. HOECKER. Well, sir, in terms of my budget, I will be coming back for the next budget request with a business analysis. Because from my particular office, I would like to compare the sister and brother financial OIGs, such as the Federal Deposit—FDIC, Treasury, to see if we are the right size or not. My sense is that we are not the right size, that we need to grow. But I am not prepared right now with a business case to ask for logical support for that, sir.

Mr. SERRANO. Okay. Thank you, Mr. Chairman. I know we have other members who want to ask questions.

Mr. CRENSHAW. Mr. Womack.

Mr. WOMACK. Thank you, Mr. Chairman. And appreciate the witness' testimony here this afternoon.

I want to go back to what the Chairman talked about just a minute ago in the case of rulemaking and particularly as it concerns the Jobs Act. We passed that nearly a year ago. And it required that rules be adopted within a year. And, of course, we know what calendar month we are in now, March of 2013. I recognize you have been on the job a short period of time. But in your brief time, can you elaborate on why it takes the SEC so long to implement rules, rulemaking responsibilities? And if this has come to the attention of the IG in the past, based on your research.

Mr. HOECKER. The only issue, sir, that has come to our attention was the economic—economic cost-benefit analysis, which was requested by the House Government Oversight Committee. That was brought to our attention.

But in terms of the agency not being able to meet the deadlines, I don't know where to go with that to give you a concrete analysis. But my sense would be that Dodd-Frank significantly changed the mission of the Securities and Exchange Commission. I don't know what that means in their world. But all I know is kind of studying right now with this job, studying for the job interviews when I was talking to the commissioners, and I do know that Dodd-Frank changed the mission somewhat in terms of adding rulemakings. And to the extent that these rulemakings and the level of effort that that is going to take, I just can't answer that, sir.

Mr. WOMACK. I think mainly what I am looking for is maybe some speculation and opinion, qualified or unqualified, based on your short amount of time as to, is it a resource problem? Is it a, for lack of a better term, a denial problem, that we are in denial that this is something that we have to perform on a certain time scale? And I suppose I would be remiss if I didn't characterize my question in the same framed context I would about the delay on getting the President's budget. Is it okay for the Federal bureaucracy to ignore the desires of Congress and miss important deadlines or timelines that we have established through our—through enacted law?

Mr. HOECKER. I think it is important that if Congress gives somebody a deadline, that they meet it.

But I also realize when you change an organization, when you change an entity, it is not easy to change, particularly if you are the size of the SEC. So I would—my opinion, which I will qualify as new-guy opinion, sir—that it would be a mixture of the appropriations level combined with changing the agency. Because I always say, when you change an agency, it is like steering a battleship. So it has to happen gradually, not that it has to, but it happens gradually. We all want it sooner. But I think the nature of change within a large organization, that is what we see.

Mr. WOMACK. Would it be your testimony that based on your initial observation that it would not be a resource problem necessarily?

Mr. HOECKER. I don't know what it would be, sir, because I don't have a body of knowledge to support that. And I would not want to kind of walk on that plank, if you will. But my sense is, I guess it would be a sense, it would be a mixture of a change, changing an agency's mission significantly, and funding it appropriately.

Mr. WOMACK. Finally, there has been a lot of talk about our potential vulnerability to cyber. And I want to just kind of throw you out on the table for you to comment about. Obviously, if our country, which is attacked every day thousands and thousands of times for various purposes, various reasons, are we pretty confident—not confident, concerned about our vulnerability from purely the SEC’s standpoint on potential cyber—cyber warfare?

Mr. HOECKER. I think we should be concerned overall, I mean, all government for the cyber warfare. I don’t think we—I think the defense is just—it takes a lot of resources, it takes a lot of skill. So I don’t think anybody’s out of the woods in terms of not being a target threat of a cyber threat.

Mr. WOMACK. Mr. Chairman, I will yield back my time.

Mr. CRENSHAW. Mr. Quigley.

Mr. QUIGLEY. Thank you, Mr. Chairman.

Good afternoon.

Mr. HOECKER. Good afternoon, sir.

Mr. QUIGLEY. I think the SEC as an agency, like most knows, it can do better. But if we are talking about the size of agency compared to the task at hand, I think it is at least fair to, as you did, notice that Dodd-Frank changes and adds responsibilities that are pretty significant and pretty important. But I also think it is fair, if we are talking about large budgets and bureaucracies, to remember who they are regulating. This is a—their budgets dwarf anything—a more fair question is can the agency possibly keep up with those companies that they are asked to oversee. Particularly with sometimes the amnesia of why we needed Dodd-Frank, what tipped off the near collapse of our financial system, in your mind?

Mr. HOECKER. Well, I do think in general, the industry is way ahead of government in terms of IT. And so if you take the IT and if you look at even high-frequency trading or things like that, where there are nanoseconds of difference, there is a catch-up for government agencies to worry about. And I think traditionally we have—we have lagged behind.

Mr. QUIGLEY. In your mind, how is the SEC doing now in their attempts to catch up on the technology side? I mean, granted, they are not going to get a big budget as they think they need or perhaps need. So can they catch up on the technology side or come closer?

Mr. HOECKER. I think they can come closer. I think they have some work to do. I don’t have specifics in terms of they need to do X, Y, and Z. But I am sure that there are some improvements they can make and should make. And as we factor in our audit planning for next year, I am sure that we can look at some of that stuff.

Mr. QUIGLEY. And in looking at the politics of cost-benefit analysis, I am sure as you oversee what the SEC tries to do, you recognize that some of these costs and the type of analysis are really hard to capture. And some of the benefits equally difficult to capture.

I mean, how much does a rule which helps protect the public’s trust in the investment system have a value? I mean, how much more does it in your mind—is it at least a difficult task to at least recognize that the public’s trust matters? And I am not sure how you quantify an element like that.

Mr. HOECKER. I am not sure how you quantify that either. But I know that the SEC has economics folks and continues to try to hire folks in that capacity. But I think the rulemaking is that you have to—you have to try and then you have to at least explain why you couldn't. And it has to be pretty clear, and to the extent that where that explanation appears is a question.

Mr. QUIGLEY. And I appreciate your attempts when you analyze those cost-benefit analysis, to take that thought into consideration. Thank you.

And I yield back, Mr. Chairman.

Mr. CRENSHAW. Mr. Graves.

Mr. GRAVES. Thank you, Mr. Chairman.

I wanted to ask a second about the process. You have submitted a budget request to, I guess, the House and I assume the Senate. Is there a timeline for which you follow to do that and all agencies, and what would that be?

Mr. HOECKER. Well, the way that works with Inspector Generals, since the 2008 Inspector General Enhancement Act or Improvement Act, I believe, is we submit our budgets to the agencies. But I say they are kind of firewalled. Because we send that to—I don't know if we really send it to the House and Senate. But there is a way that they are not supposed to touch our budgets. And that goes in with the regular budget process itself. So we don't have a different timeline as an Inspector General's Office than the agencies. So we fall in line with the agencies.

Mr. GRAVES. What is the timeline for the agencies to submit theirs?

Mr. HOECKER. Well, typically, we—I believe it is in January, provide that to the agency. And then the agency has a certain timeline to submit that to OMB. And I don't know what the SEC has.

Mr. GRAVES. But they submitted theirs on time, I assume.

Mr. HOECKER. I have to assume, but I don't know for sure sir.

Mr. GRAVES. When they submit it, they are submitting it to OMB, which, in essence, is to the administration for the preparation of their budget request.

Mr. HOECKER. Yes, sir.

Mr. GRAVES. So it is probably fair to say that OMB or the administration has all the agencies' budget requests in place and they have just themselves chosen not to compile that and deliver that to the House and Senate in a timely fashion.

Mr. HOECKER. I am not sure how that works. But OMB assembles all the agencies' budgets and puts it all together. But I am not sure who didn't send it or who didn't compile it.

Mr. GRAVES. Okay. Understand. I have just another question. In your written statement, you referenced "The Misuse of Government Resources." A report that had come out recently. And it was in reference to about a million dollars of wasteful spending on computers and software without any oversight or planning of the use. In that, you know, certainly that is something we are interested in, is something such as that.

What was the result of that? And—or maybe, first, in your—in the report why was there all of a sudden a surge in spending that was wasteful and the equipment was never used and there was no planning for it?



Mr. HOECKER. I don't have those details before me right now. I know the case you are talking about. We did an investigation. I know that the SEC management took—took pretty quick action. I don't know what action that is because I have been briefed at a high level. If you want it, my staff can get back to you or I can get back to you on that issue.

Mr. GRAVES. To your knowledge, was anybody terminated or held responsible for the misuse?

Mr. HOECKER. I don't have any knowledge of that right now.

Mr. GRAVES. Was that something you could find out for us?

Mr. HOECKER. Absolutely. Absolutely.

I have just been told that two individuals have resigned as a result of that.

Mr. GRAVES. Two individuals resigned.

Mr. HOECKER. But I will follow up more completely with you.

Mr. GRAVES. As, you know, the inspector general, in the future, do you feel that that is sufficient penalty or recourse that two individuals resigned as a result of a million dollars of taxpayer dollars being misused?

Mr. HOECKER. As inspector general, when I do an investigation that involves misconduct on an individual, I am a factfinder. And my reports either state that it appears that this person violated this regulation or this law, but we don't—we don't recommend what discipline to take. In other words, this means termination, this means a letter of reprimand, because that is outside the factfinder, and that would be going outside of the independence issue for an inspector general to do that, in my mind. But the agency has to take appropriate action. And as there are a number of things they look at when they get a report such as ours, they look at the Douglas factors, they look at past records, and they look at similar actions that they have taken.

So that is—that is totally the agency's call.

Mr. GRAVES. Okay. Thank you.

Thank you, Mr. Chairman.

Mr. CRENSHAW. Mr. Diaz-Balart.

Mr. DIAZ-BALART. Thank you very much, Mr. Chairman.

How are you, sir? By the way, good staff work there on that issue.

The report, which is called, "OIG's Follow-Up Review of Cost-Benefit Analyses in Selected SEC Dodd-Frank Act Rulemakings," I understand it is not a catchy title, but that is exactly what it was.

Mr. HOECKER. Yes, sir.

Mr. DIAZ-BALART. It states that the SEC is not providing, frankly, a full picture of whether the benefits of a regulatory action are likely to justify its cost and discovering which regulatory alternatives would be more effective.

Now, we do know that many SEC rules have been challenged successfully, frankly, in court due to poor analysis by the SEC in its rulemaking process. There are a few examples of those, including, for example, the proxy access rule. Three quick questions for you, if I may. By the way, it also states in that report that the SEC rarely factors in internal costs to the agency during its rulemaking process, which obviously, it would seem to me, is an important factor that they are leaving out. Three questions.

Since that report was published, do you know if the SEC has made any efforts to change their cost-benefit analysis? You know, what are they doing to improve their rulemaking process?

Mr. HOECKER. Yes, sir. I believe that that report, which is No. 499, that was done—when the SEC first committed to do cost-benefit analysis, there was a shorter memo by the General Counsel's Office, not the current general counsel, but the previous. And that was, like, 2 or 3 pages.

When the IG's office did this review, the one with the long title that you said, and I will just call it 499 because that is the report number.

Mr. DIAZ-BALART. That is actually catchier.

Mr. HOECKER. Yes, sir. They looked at that as the standard. So that was the criteria that they used when they did the review. And as a result of that, the General Counsel's Office issued this March 2012 cost-benefit analysis guidance. And on that guidance, the March 2012 guidance, that is what we are doing the phase 1 and phase 2 work on currently, sir.

Mr. DIAZ-BALART. Great. Great.

Do you expect or how effective do you expect that the SEC's examination process—I don't know if you are aware of this proposed Municipal Advisor Rule.

Mr. HOECKER. I am sorry, the what, sir?

Mr. DIAZ-BALART. Municipal Advisor Rule. Let me just throw out a couple questions, and I figure that you might not be—so here is the issue. This rule, which I am concerned whether they are listening to the relevant industries that they are dealing with—this is in general—are they listening to the relevant—you know, the industries that they are about to regulate, they are regulating, and to the public during their rulemaking process? That is one question. That would be my second question. And also, how effective is their examination process for—in this new process, which I guess I can speak to your staff as well about. But are they listening to this very large number of new registrants that are expected under the very broad scope of this proposed Municipal Advisor Rule? And I can get your staff more detail. But I just want to see if there are, in fact, if they changing their way a little bit. Are they speaking to folks? Are they listening to folks? And how effectively are they doing it? Or are they just kind of going through the motions?

Mr. HOECKER. I don't have a body of knowledge to support any answer to that. I do know they have public hearings. I don't know if we have looked at the effectiveness of those. But what I would like to do is to see if we can somehow get back to you on it and have my staff provide a written answer to those questions, to the best we can, sir.

[CLERK'S NOTE.—The information follows:]

As you know, Section 975 of Title IX of the Dodd-Frank Act, entitled, “Investor Protections and Improvements to the Regulations of Securities,” amended Section 15B of the Exchange Act to require municipal advisors to register with the Commission. Specifically, the revised Section 15B made it unlawful for a municipal advisor to provide advice to or on behalf of a municipal entity or obligated person with respect to municipal financial products or the issuance of municipal securities, or to undertake a solicitation of a municipal entity or obligated person, unless the municipal advisor is registered with the Commission.<sup>1</sup> To enable municipal advisors to temporarily satisfy this requirement, the Commission had adopted an interim final temporary rule and form that will expire on December 31, 2011. The Commission has proposed new rules and forms under the Exchange Act to give effect to the provisions of Title IX of the Dodd-Frank Act that, among other things, would establish a permanent registration regime for municipal advisors and impose certain record-keeping requirements on them.<sup>2</sup>

The SEC’s Division of Trading and Markets (TM) led this rulemaking on registration of municipal advisors, and the SEC sought comment on all areas of the proposal, including estimates of the costs and benefits identified in the economic analysis section of the proposing release and any costs and benefits not discussed in the release. TM relied heavily on the SEC’s Division of Risk, Strategy, and Financial Innovation (RSFI) to determine those areas on which comments should be solicited.

The comment period ended on February 22, 2011, and approximately 900 comment letters were received as of June 3, 2011, including several on the economic analysis section.<sup>3</sup> As stated in the OIG’s initial review of the SEC’s application of Cost-Benefit Analysis in Rulemakings, most of the comments received on the economic analysis section related to the specific Public Records Act (PRA) costs associated with the registration requirement. This may have been due to the focus of many of the comments on who would be required to register under the proposed rule. Specifically, many commenters interpreted the release to require all appointed officials of municipal governing bodies to register as municipal advisors, despite the fact that the scope of the proposed regulation was not that broad.

During the OIG’s review, the TM staff stressed that all comments are reviewed and that even one comment on a particular topic would be considered in determining what changes to recommend to the Commission in the final rule.

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<sup>1</sup> Registration of Municipal Advisors, Proposed Rule, 76 Fed. Reg. 824, 825 (Jan. 6, 2011).

<sup>2</sup> *Id.* at 824.

<sup>3</sup> Copies of comments received on this proposal are available on the SEC’s website at <http://www.sec.gov/comments/s7-45-10/s74510.shtml>.

Mr. DIAZ-BALART. That would be great. And I think my staff, Ryan Canfield, who is here, will probably be able to touch base with them and get them talking.

Mr. HOECKER. Okay. Thank you.

Mr. DIAZ-BALART. Thank you, sir.

Thank you, Mr. Chairman.

Mr. CRENSHAW. Thank you.

Mr. Yoder.

Mr. YODER. Thank you, Mr. Chairman.

Welcome to the committee, sir. Glad you are here.

Wanted to discuss the changes made in the last couple of years regarding Dodd-Frank. It has been mentioned a couple times already in the hearing. I note that the SEC had some of its responsibilities transferred to the Consumer Finance Protection Bureau. I guess I would like you to discuss that a little bit, what that transition has been like. Have we determined whether these changes were good changes on policy grounds, those sorts of things; have we had any sort of determination of whether these things have moved in the right direction? Has the transition worked?

And then, I guess, secondly, as these responsibilities are transferred, do we show dollar-for-dollar savings, such that we are not leaving behind duplicative costs in the SEC? If we are transferring responsibilities over, that should be a reduction in expenditures of the SEC, and have those been fully received?

Mr. HOECKER. Well, sir, that is a great question, and particularly in terms of your second part, reporting the savings. I don't have any knowledge to answer that question right now. And I would ask that maybe you allow me to get back to you on that.

[The information follows:]

Upon further review following the March 2, 2013 Appropriations Hearing, my staff was unable to find examples of responsibilities that were transferred from the SEC to the CFPB as a result of the Dodd-Frank Act or otherwise. Accordingly, my office could not identify any associated costs savings or ancillary benefits that may have been incurred by the SEC by a reduction in regulatory responsibility.

Mr. YODER. Okay. That would be great. And certainly, as we go forward in the hearings in the next coming weeks, be a good opportunity to discuss that with the SEC, and we would love to have your background on that first.

I appreciate that.

I note some conversation about the ability for the SEC to focus on the right priorities. And whether they are able to move the rules forward in an appropriate manner and a timely manner. And I have noted that the SEC is now considering proposing rules about political campaign contributions that were not necessarily mandated by Congress. Are we in a position where our mandated responsibilities are not being met but our responsibilities that the SEC has sort of volunteered to take on are being met in a higher priority? Can you explain how we are dealing with that and whether those responsibilities are being properly, I guess, moved forward on?

Mr. HOECKER. I think the larger area on that would be if you have X-amount of rulemakings are you—and those are required under Dodd-Frank, are you working on those, or have you added some other rulemakings? And that, again, sir, has fallen into an

area where I just don't have the knowledge yet. What I do know, and the rule that you are speaking of, I think they are considering it right now. I don't know what—exactly what progress, but I think it is more in the proposal stage right now. But I don't know how much effort they have spent in doing that.

Mr. GRAVES. If you could report back on where they are and the political disclosure rule and the determination of the cost of that, how they are proceeding and maybe an analysis of the impetus behind that. This is not a Congressional direction; so what is driving that? What is thrusting that? And how it is affecting their ability to move forward on their mandated rules under Dodd-Frank, which certainly small businesses, the committee economy is waiting on certainty? So any of these things that are outside of that purpose are going to make it more difficult to do what everybody on this committee wants to do, which is get the economy going again and creating jobs. So we need the SEC to, obviously, be a partner in that. And these other items tend to take away from that. Would love to get some background on that as well.

Mr. HOECKER. Okay, sir.

[The information follows:]

Our office does not have an independent body of work or evidence to suggest that the Securities and Exchange Commission (SEC or Commission) has prioritized discretionary rulemakings over Dodd-Frank or JOBS Acts required rulemakings. However, as we continue our audit of the SEC's application of cost-benefit analysis during the SEC's rulemakings continues, we will keep these concerns in mind and report any contrary information we find.

Mr. YODER. Mr. Chairman, I yield back.

Mr. CRENSHAW. Thank you. I think we will have time if other questions are on people's minds, we will go into a second round of questions.

And I will start by asking you, the oversight that you are in charge of, some of your predecessors have focused on the investigation side; some have focused more on the audit side. As I understand it, you have got maybe a third way to look at things, and that is through a kind of evaluation, which seems to make sense as you conduct that oversight.

And in that regard, I wanted to ask you about some of the settlements that have taken place and what your plans are. You read from time to time where Federal judges will throw out a settlement that SEC has reached with a defendant. I saw one the Federal judge threw out and he said the settlement was neither fair, nor reasonable, nor adequate, nor in the public interest.

I think that the thrust of that theory is that when SEC brings a lawsuit against someone, a bank or whoever, that they think has violated a law, after an investigation, and a settlement is reached, and there is no admission of guilt. Judges have taken a position that, well, if they really haven't found any facts, there is nothing to base the settlement on; then maybe it is not a legitimate settlement. This is going to create a little bit of havoc, I think, in terms of these settlements. I know that SEC has been criticized from time to time for just entering into settlements, never really going to trial. I am sure they would argue if they are against some big corporation, they don't have the time, the energy, and the money to

actually pursue a full trial and end up with a judgment, which may or may not be true.

But I just wonder, from your standpoint what you think, since I think that is going to be the subject of conversation, even though it is really more of a question in terms of priorities with the new Chairman. But as the inspector general, is that something that you think you would look into just—I guess you would look into the enforcement part of the SEC, just to take a look and see how the settlements are made and whether that is good business or bad business? Is that something you think you might pursue?

Mr. HOECKER. Well, sir, the evaluation, to kind of address the first part of it, you are right. There is a third kind of pillar, if you will, in the IG community, that is evaluations. And that is somewhere between audit and investigation. It is usually a shorter duration, a more limited kind of scope or objectives. And I would think, in terms of any kind of metric that enforcement might use, we could do some kind of an evaluation in terms of analyzing what their metric was, how they achieved that. And if the metric deals with settlements, and I am not sure what that would look like, but if there are some trends where settlements are as you describe, then that would come out in that type of an analysis.

Mr. CRENSHAW. Got you. Thank you. Let me ask you a question about leases which seem to be problematic for the SEC. I think I mentioned in my opening statement that since 2001, we have actually doubled the amount of appropriations the SEC has. And they have had some extra regulatory authority as well. What we all want to make sure is that the money that we appropriate is spent wisely. And when it comes to leasing, the SEC hasn't done all that well. I know they are working through all that. But if you spend your money wisely, you have got more money to spend, obviously, if you don't waste it.

But with all this—the lease that took place and then GSA came in all that is getting worked out. But the bottom line is that SEC leased a whole lot of space that they ended up not needing. I think I read there are 500 work stations in that new facility that aren't being used. So is that something that you are going to look into? I don't know what the final answer to that is. But I imagine that it is something that your office would review and probably be better able to tell us if the space is being wasted or if they have got plans to utilize the space. Is that something you have had a chance to look into or planned on looking into?

Mr. HOECKER. I do know that the SEC OIG had done a review that kind of exposed that, if you will, and that the SEC is consolidating some things. I believe there is a facility in Alexandria they are moving into headquarters, to fill that space and get that ratio more in to conformity with the GSA requirements of if you have a certain grade of an individual, they would get X amount of square feet as an office. I do know that they are working toward that. As they work toward that and when they feel that they have kind of done what they can, I think that is something that my office could do a follow-up audit and figure out where they are and report out on it, sir.

Mr. CRENSHAW. That would be great.

Mr. Serrano.

Mr. SERRANO. Thank you, Mr. Chairman.

Sir, your testimony provides several examples of investigations that your office has conducted. And in almost all of these examples, the SEC has concurred with all of your recommendations, which is commendable, if not surprising, right, for any agency.

It seems you have a very good relationship with the SEC. And I wonder if you could tell us about that relationship and tell us, in fact, if that is necessary. You know, when we think of an inspector general, many people see sort of a watchdog over an agency. So is it important to have—first of all, what is your relationship to them? And is it important whether or not you have a good one?

Mr. HOECKER. Well, sir, that—to address that is the previous relationship that they concurred with all of the audits. But I realize your question deals with me and the value that I—that I have on the relationship.

I think a positive relationship helps. When I was the IG of the Capitol Police, I had a very positive relationship with the Chief of Police and the Capitol Police Board. I think that just facilitates things. Because when you talk about change management, positive change management, the higher up the executives are involved, then that just helps that whole change.

My expectation of the relationship is that I don't ever expect to be invited to anybody's Christmas party as an IG. I just don't, because that is not the purpose of an IG.

Not that I wouldn't go to anybody's Christmas party and not that I am soliciting Christmas party invitations, but it doesn't break my heart that people aren't calling me. Just checking up on me, are agency management saying, "Hey, how you doing?" I just don't have that expectation as an inspector general. And part of that may be just my upbringing in law enforcement is the same way.

But I intend to have a constructive relationship. I intend to meet the commissioners on a regular basis. I intend to meet the office and division directors on a regular basis, just to share what work I can share with them, just to resolve some issues, like recommendations. Because I think we probably all want change. So if I find something in an audit or an investigation, the facts are the facts. I think we pretty much agree on the facts. It is the fix that really is the agency's responsibility. And to the extent that the recommendations could better address a fix to a situation, then that is just—and then that just makes it easier for the agency and more appropriate for the agency, because it is their responsibility. So not that they would change any of the outcomes of my report. But just in my job in meeting these—meeting the execs are to share with them what I found and to get buy in that this is a problem and it warrants sufficient attention to change. And that is the kind of way I practice being an IG, sir.

Mr. SERRANO. That certainly makes sense. And if you are short on Christmas parties, Mr. Crenshaw is—and the other guys would probably have a few around the time.

We will probably still be in session so you probably can just come to one of our own.

As the IG, you have a unique perspective on the agency's readiness for the work of Dodd-Frank. As you know better than most, the additional responsibilities are numerous, but the staff has not

been significantly increased to deal with these responsibilities. I know again that you have been there a short time. But what are the consequences in your opinion of flat budgets in this important time of rulemaking?

And, by the way, we want to be clear on something—at least I want to be clear on something. There is a big difference, as you know, of opinion in Congress as to what is wasting money and what is investing. So we don't want you to get caught up and having to sound like you are taking sides on that. But then your role is to see that they do what they are supposed to do, and at times, you also have an understanding of what they need to do. So based on that, as we ask them to come up with all of this work, can these flat budgets affect or—once before, you said they will have to make it work. But I want you to go a step further than that. You know, of course, they will have to make it work. But could their life be easier in doing what they have to do?

Mr. HOECKER. When I said make it work—you are right. So there are only so many weekends you can work if you have X amount of things to do, whether that be Dodd-Frank or something else, another requirement.

Requirements cost money, investments, as you say. And as somebody who runs an office, I will take all the investments I can get, so to speak. In other words, you know, if there are investments to be made then in my office, there are investments to be made in the Commission, then I think we should do it. I just don't think I am in a position to say that they have these, say, 10 items, for example, and they can only do 8 because of the certain level of budget. I just don't have that knowledge, sir. And that is really not something that an IG would do in terms of analyzing a budget that is submitted to OMB.

What we would do is we look at, so, slices of the appropriations, slices of the funding to make sure that if, for example, in the leasing, if we don't think they are spending money wisely in a leasing situation or if we think they wasted money on IT, then this is something we would look at and report out on it.

Mr. SERRANO. I understand that. That is clear to me. But the time may come when, as you look at how they are spending money, and you are looking to make sure there is no waste, you also see shortcomings. And we would hope that whether or not it is the role of the IG, I am sure it can be interpreted as such that you see what is going on later on.

Mr. Chairman, I want to make a suggestion, which is probably very unpopular. But it is clear that 4 weeks on the job is not nearly enough time to know all that is going on that one needs to. Yet we know because of Dodd-Frank, because of the Jobs Act, because of all of the issues on both sides of the aisle, the SEC will be an agency under a lot of Congressional scrutiny. So maybe we should establish something where we keep in touch with this particular IG. I am not suggesting another hearing. But as the session goes on, and as this 2-year term goes on, because I think the SEC will be in the forefront of a lot of questions being asked by both sides.

Mr. CRENSHAW. I think you are exactly right. And I think when we have—hopefully, a budget or even if we don't get a budget from the executive branch, we will probably have a hearing where the



new Chairman of the commission will be before us, and we will ask some of those questions. And really appreciate his being here as new on the job.

But I think some of the things that we are talking about are things that you are going to be looking at. You have immersed yourself in it already.

But you are exactly right. The areas where he is finding that there are inefficiencies, then we want to hear about. And the areas where he thinks the SEC is doing a great job, we certainly want to hear that as well. So I think there will probably be an opportunity, if and when we have a chance to talk to the new Chairman. But certainly we will stay in touch. And, again, we appreciate the fact that just 30 days ago, you were put on the job. I think you have evidenced a really good understanding of what the issues are, particularly as they relate to your role as the overseer.

Mr. SERRANO. I remember when came to Congress in a special election, I walked in to get my voting card. They said, "Go vote." I said, "What are we voting on?" It was the military action on Panama. It is costing a few dollars. I said, "Oh, that is all?"

Mr. CRENSHAW. That is all.

Now I call on Mr. Graves.

Mr. GRAVES. Thank you, Mr. Chairman.

Well, I would say, I mean, if 30 days in the position, you have done a great job of grasping many of the issues that the panel has put forward today. I have another, and I hope you have a little insight into it. And if you don't, certainly would welcome a followup. But part of Dodd-Frank, and Dodd-Frank has impacted so many areas and so many elements throughout the financial sector. One was addressing streamlining the SEC. And it provided for the fact that a study must be done in which to streamline. And a group was contracted to do that, spent 6 months going through the process, and made many positive recommendations. And it is my understanding that maybe some of the recommendations have been implemented, but, for the most part, many have been ignored, and commonsense things: combining areas of interest and consolidating various departments and such, things like the private sector would do on a regular basis in order to streamline and be more efficient. But the SEC seems to be rebuking the recommendations that the law required that there be some recommendations of streamlining.

So what can you do to ensure us, looking ahead, that the IG will be really aggressive in pursuing the full implementation of positive recommendations of efficiency and streamlining here.

Mr. HOECKER. Well, sir, I am aware that they did hire a consulting group to make those recommendations, and I believe there was an implementation contract, and they are working some of those implementations. The degree of completion I am not aware of, but this is something that we definitely could consider in terms of a project to follow up on at some point and figure out of all the implementation or of all the recommendations of that first consulting group, what have we done? It is something we could definitely follow up on.

[The information follows:]

Our office does not have an independent body of work to draw from in order to opine on the issues associated with full implementation of BCG's recommendations.

However, we note that the SEC, in its the three status updates in response to the BCG recommendations, represents that a majority of the recommendations been implemented.

Mr. GRAVES. Yes, that would be good to do, because it is my understanding that nearly \$5 million was spent on a report and a study, and I consider that a significant sum of money, to put forward a report to create more efficiency within an agency, or a commission in this case, and just to ignore the results, what does that tell our constituents back home? And why would this body go to such effort to put forward the thoughts and the ideas and allocate and appropriate the money to do that if it is just going to be ignored?

So I certainly would welcome your follow up, in particular your plans and holding them accountable in the implementation of the streamlining and efficiency report recommendation.

Mr. HOECKER. Yes, sir. I know they have done some of the implementations, but I don't know the extent. Like you say, there is probably some more out there that they need to fully implement that they have not. We will be glad to look at them and report out on them, sir.

[The information follows:]

The implementations of BCG's recommendations are not a programmatic function managed by the OIG. However, the OIG notes that the BCG report, issued March 10, 2011 provided 20 initiatives designed to increase the SEC's efficiency and effectiveness. As stated in the SEC's Third Report in the Implementation of SEC Organizational Reform Recommendations, the SEC established the Mission Advanced Program (MAP), which provided the framework for evaluating and implementing the changes. The BCG approaches were assigned to working groups composed of Division and Office executives and staff. As further stated in the report, 15 of the 20 initiatives examined have been completed and the implementation phase is complete or in process for each.

Additionally, as I began my tenure as the Inspector General of the SEC, the office I encountered has talented staff that had been without a permanent leader for over one year. The key senior leadership positions of Deputy Inspector General and the Assistant Inspector General for Investigations were vacant, as well as six staff positions. Unfortunately, the office is also faced with a pending litigation brought by a former employee requiring every staff member in the office to be responsive to discovery requests and, most likely, depositions. This is truly a situation where OIG cannot successfully carry out its mission.

Accordingly, My top priorities for this year are to:

- Complete the two audit reports on cost-benefit analysis requested by the House Government Oversight Committee.
- Complete other statutorily required work.
- Hire the two leaders (Deputy Inspector General and Assistant Inspector General for Investigations).
- Fill the remaining vacant positions.
- Continue to investigate complaints of misconduct reported to OIG.
- Complete the process of rebuilding the OIG.
- Determine what audit work can be done for the remaining fiscal year.
- Complete an audit plan for next fiscal year.
- Be responsive to future Congressional requests for information including but not limited to review of the SEC's implementation of the BCG recommendations.

Mr. GRAVES. Thank you.

Mr. CRENSHAW. Just a comment on that last question, the consulting group said, I think, for instance, that the SEC doesn't currently have a clearly articulated agency-wide strategy for its regional office presence, just as one of the areas that they need to work on, so I think that is something you all can kind of follow up with.

Mr. Diaz-Balart.

Mr. DIAZ-BALART. No questions.

Mr. CRENSHAW. Mr. Yoder, do you have any more questions?

Mr. YODER. Just one quick one, Mr. Chairman. Thank you.

Just one issue, Mr. Inspector, I wanted to raise that you might look at when conducting your efforts. In your testimony, on page three, you note that the SEC is subject to various statutory requirements to consider a proposed rule's, quote, "effects on competition and the needs of small entities." I am concerned the SEC did not consider small entities when it proposed the conflict minerals disclosure rule and is failing to consider small entities' unique compliance needs now that the rule is final.

We have dealt with some small companies in my district that have some real challenges being able to really comply with those rules and a business locally that was contacted, a small business that makes voting machines, surgical drills, and fitness equipment, in my district that was contacted by one of their publicly traded clients who needed disclosure about their use of conflict minerals and they have no idea how they would begin to comply.

I brought this up last year with the SEC and I don't think we have gotten to the point where we are adequately resolving what to do about small companies with the burden that is unmeetable. My hope was that we could have some sort of de minimus rule that could be created that would give these companies an opportunity to comply if they meet a certain threshold, and we believe that is within the SEC's jurisdiction to create such a rule.

Mr. HOECKER. Okay. Thank you.

Mr. YODER. Thank you, Mr. Chairman.

Mr. CRENSHAW. I don't haven't any further questions.

Mr. Serrano, do you?

Mr. SERRANO. I don't, and whatever questions we may have, we will submit for the record.

Mr. CRENSHAW. Mr. Hoecker, just let me thank you again for your testimony, for being here, baptism by fire. We appreciate that.

Thank you, Members, and I look forward to our next hearing. This meeting is adjourned.

**Financial Services and General Government Subcommittee**  
**Oversight Hearing - Securities and Exchange Commission**

**Questions for the Record Submitted by Chairman Ander Crenshaw**

***Rulemakings***

I am concerned about the prioritization of rulemakings that the Commission has undertaken. For example, the Commission still has a number of rulemakings required by both Dodd-Frank and the JOBS Act outstanding, but it has prioritized non-statutorily required rulemakings above these.

**Question: Do you think this is appropriate?**

**OIG Response:** Our office does not have an independent body of work or evidence to suggest that the Securities and Exchange Commission (SEC or Commission) has prioritized discretionary rulemakings over Dodd-Frank or JOBS Acts required rulemakings. However, as our audit of the SEC's application of cost-benefit analysis during the SEC's rulemakings continues, we will keep these concerns in mind and report any contrary information we find. Additionally, as agreed during the March 12, 2013 hearing, our office will inquire into the impetus behind the SEC's Division of Corporate Finance's decision to post an agenda item with the Office of Information and Regulatory Affairs, Executive Office of the President that stated, "The Division is considering whether to recommend that the Commission issue a proposed rule to require that public companies provide disclosure to shareholders regarding the use of corporate resources for political activities."

Your office has looked at the Commission's use of cost-benefit analysis in their rulemakings and found them lacking in some areas.

**Question: Has the Commission been responsive to the suggestions from your office?**

**OIG Response:** Yes, the SEC has agreed to implement all recommendations made by our office regarding the use of cost-benefit analysis in rulemakings.

**Question: Were there areas of disagreement? If so, please explain.**

**OIG Response:** On January 27, 2012, the OIG issued a report titled, "Follow-up Review of Cost-Benefit Analyses in Selected Dodd-Frank Act Rulemakings." This report was the second report issued relating to cost-benefit analyses conducted by the SEC for Dodd-Frank rulemakings.

In the follow-up review, our objectives were to: (1) assess whether the SEC was performing cost-benefit analyses for rulemaking initiatives that were statutorily required under Dodd-Frank in a consistent manner and, (2) determine whether problematic areas existed where rigorous cost-benefit analyses were not performed and where improvements were needed and best practices could be identified to enhance the overall methodology used to perform cost-benefit analyses.

In the follow-up review which culminated in the January 27, 2012 report, the OIG found that although the SEC is not subject to an express statutory requirement to conduct cost-benefit analyses for its rulemakings, it is subject to statutory requirements to consider factors such as the effects on competition and the needs of small entities. The OIG further found that the SEC must generally also provide the public with notice of, and opportunity to comment on, its rulemakings.

Our report listed several recommendations for improvements to the SEC's practices. These recommendations were: (1) considering ways for economists to provide additional input into cost-benefit analyses of SEC rulemakings to assist in including both quantitative and qualitative information; (2) reconsidering the approach that the SEC only perform cost-benefit analyses for rulemaking activities to the extent that the SEC exercises discretion and considering whether a pre-statute baseline should be used whenever possible; (3) using a single, consistent baseline in the cost-benefit analyses with such baseline being specified at the beginning of the cost-benefit analysis section; (4) discontinuing the practice of drafting separate cost-benefit analysis and efficiency, competition, and capital formation sections and instead provide a more integrated discussion of these issues in rule releases; (5) directing rulemaking teams to explicitly discuss market failure as a justification for regulatory action in the cost-benefit analysis of each rule; and (6) including internal costs and benefits in the cost-benefit analyses of rulemakings.

SEC management concurred with all but one of the report's recommendations, number five, and indicated that they welcomed the constructive recommendations for improvements to SEC practices. And, as stated above, have implemented all of the recommendations, including recommendation number five.

**Question:** Do you believe the SEC has enough economists on staff who are properly trained to do the kind of economic analysis that is critical when making these kinds of rulemakings?

**OIG Response:** Responding to a request from several members of the U.S. Senate Committee on Banking, Housing, and Urban Affairs the SEC OIG conducted a review of the cost-benefit analyses performed by the SEC in connection with six specific rulemaking initiatives pursuant to Dodd-Frank.

In the June 13, 2011 report titled, Report of Review of Economic Analysis Performed by the Securities and Exchange Commission in Connection with Dodd-Frank Act Rulemakings, the OIG concluded that the SEC had conducted a systematic cost-benefit analysis for each of the six rules, but found that the level of involvement of the Division of Risk, Strategy and Financial Innovation (RiskFin) varied considerably from rulemaking to rulemaking.

The OIG conducted a follow-up review in which the OIG examined in greater detail the cost-benefit analyses the SEC performed and retained an expert, Dr. Albert S. Kyle to assist with the review. On January 27, 2012, the OIG issued the follow-up report titled, Follow-up Review of Cost-Benefit Analyses in Selected Dodd-Frank Act Rulemakings, wherein we concluded that a systematic cost-benefit analysis was conducted for each of the six rules reviewed. Overall, we found that the SEC formed teams with sufficient expertise to conduct a comprehensive and thoughtful review of the economic analysis of the six proposed releases examined. Our review

noted that Dodd-Frank requires the adoption of many different required regulations that create costs and benefits which spill over into other SEC promulgated regulations. Therefore, we concluded it was critical to have cost-benefit analysis coordinated by one group of economists, who can ensure that the costs and benefits of proposed rules are not ignored or double counted.

Based on the results of that review, the OIG made six recommendations including that SEC rule writing divisions and RiskFin should consider ways for economists to provide additional input into cost-benefit analysis of SEC rulemakings to assist in including both quantitative and qualitative information to the extent possible. The report further noted that economists do play a significant role in the SEC's cost-benefit analysis, but that their expertise is being stretched thin.

### ***Onerous/Outdated Regulations***

Executive Order 13563 requires agencies to review regulations and eliminate outdated or overly burdensome regulations. As an independent agency, the SEC is not bound by this order. However, I think everyone would agree that outdated and burdensome regulations should be eliminated.

**Question:** Is this an area that your office has looked into?

**OIG Response:** Our office does not have an independent body of work from which to respond, however, and as noted above, SEC Chairmen have made a commitment to Congress that the SEC will conduct cost-benefit or economic analyses in connection with its rulemaking activities. Specifically, according to Office of the General Counsel (OGC) officials, former SEC Chairman Arthur Levitt stated that there was an expectation that the SEC would perform cost-benefit analyses as part of the rulemaking process. In fact, the Commission's current rulemaking procedures are closely aligned with the requirements of EO 12866, EO 13563, and OMB Circular A-4, as indicated by the following statement on the SEC's website:

While [EO 13563] does not apply to independent agencies like the Commission, we share its goals, and many of our existing practices are consistent with those described in the Order. For example, we take into account benefits and costs in our rulemakings, assess alternative regulatory approaches, afford the public a meaningful opportunity to comment on our proposed regulations through the Internet, and coordinate our rulemakings with other agencies to harmonize regulations.

**Question:** If not, would this be something you would be interested in looking into?

**OIG Response:** OIG is always interested in conducting work responsive to Congressional interests. In determining the priority and sequence of our work, we consider, among other things, the standard, law, or other criteria requiring the SEC to carry a program or operation. As previously noted, the SEC is not required to follow provisions of Executive Order 13563.

### ***Regional Offices***

The Boston Consulting Group (BCG) report, which was required by Dodd-Frank, stated: “The SEC does not currently have a clearly articulated agency-wide strategy for its regional office presence.” The report recommended that the Commission define their approach to determine whether to retain the current regional office structure or change it. The Commission currently has 11 regional offices, but I am wondering if they need all of them. Specifically, I wonder why the SEC needs a Salt Lake City office with jurisdiction over only one State, when the average office has jurisdiction of around 5 States.

**Question:** Has your office considered looking into the structure of the Commission’s regional offices?

**OIG Response:** The OIG has not reviewed the Commission’s regional office structure and we cannot offer an opinion. However, we agree that the BCG’s finding that the SEC should have an articulated approach to its regional office locations, particularly as leases come up for renewal, is a sound management practice.

For instance, I am wondering if it would be prudent to look at when the lease for the Salt Lake office expires and consider consolidating the office to save funding.

**Question:** Is this something your office would be interested in looking into further?

**OIG Response:** This is certainly an area our office will consider for audit or possible evaluation as that program is developed in my office.

### *Improper Destruction of Documents*

As the agency in charge of making sure companies do not improperly destroy records, it is deeply concerning that the SEC was found to have been improperly destroying records related to SEC investigations for almost 20 years. I know your office conducted a review of the matter and made a number of recommendations.

**Question:** What procedures has the SEC put in place to make sure this does not happen again?

**OIG Response:** The OIG issued Report No. 505, SEC’s Records Management Practices, to the SEC on September 30, 2012 detailing the results of our audit of the SEC’s records management practices. The final report contained 12 recommendations with which the SEC’s Office of Support Operations, within the Office of the Chief Operating Officer, fully concurred and have implemented.

Additionally, as noted in the October 5, 2011 report of investigation, Case No. OIG-567, the OIG found that the SEC was following the NARA approved document retention schedule for documents relating to SEC investigations during the above referenced period. However, the above referenced OIG investigation did find that for at least 30 years, the SEC Division of Enforcement (Enforcement) has utilized Matters Under Inquiry (MUIs) as “pre-investigation inquiries.” Also as noted in the report, it is very important to note that MUIs are distinct from formal investigations in Enforcement and are “opened to collect and analyze information to



determine whether an enforcement investigation should be instituted.” Our investigation found that it had been the policy of Enforcement, from the point of time in which MUIs were first utilized until July 20, 2010, to dispose of all documents relating to a MUI that were closed without becoming investigations. This policy was publicized on the SEC’s intranet since at least 2001.

Since the release of the report, the SEC has continued to work with NARA to receive final approval of its document retention schedule for MUIs. The OIG understands that NARA has granted preliminary approval, but that the public comment period had to be restarted as a result of some of the comments received during the first round of public deliberations.

**Question:** Do you know if the SEC has been working with the National Archives to keep all documents that are required by Federal statute to be preserved?

**OIG Response:** Yes, as discussed above.

**Question:** Have all of the recommendations been implemented?

**OIG Response:** Yes, all twelve recommendations from the aforementioned audit and the five recommendations from the above referenced investigation have been implemented.

### ***Council of Inspectors General on Financial Oversight (CIGFO)***

You are part of the Council of Inspectors General on Financial Oversight which was established by the Dodd–Frank Act. I understand your office is working on a follow-up to the joint report issued by the Council last year examining the SEC’s controls for handling and safeguarding non-public information from unauthorized disclosure.

**Question:** Can you tell this Subcommittee anything about this report?

**OIG Response:** The CIGFO Annual Report includes discussions of current and pending joint projects of CIGFO members. In addition, the report includes sections, developed by each IG and under his or her exclusive editorial control, that establish a baseline of oversight activity conducted. The SEC OIG issued a report addressing controls that the SEC employs to ensure sensitive non-public information it collects from CIGFO is properly safeguarded.

**Question:** Are there any specific concerns your office has on this issue?

**OIG Response:** In the report, SEC’s Controls Over Sensitive/Nonpublic Information Collected and Exchanged with the Financial Oversight Council and the Office of Financial Research, issued March 25, 2013, the OIG found that SEC employees and contractors who access the SEC’s e-mail system using Outlook Web Access (OWA) are not restricted from saving and uploading sensitive or nonpublic information on non-SEC computers. Consequently, sensitive or nonpublic information could potentially be disclosed to unauthorized persons.

Additionally, the SEC has not appointed primary information owners to oversee information it receives and shares with the Financial Stability Oversight Counsel (FSOC), its member agencies, or Office of Financial Research (OFR). In addition, a protocol for inventorying and ensuring documents are appropriately marked has not been fully developed. As a result, the SEC may be unable to efficiently identify information owners and ensure documents are tracked and marked as appropriate.

This report contains five recommendations, with which the SEC has concurred, that were designed to improve the SEC's controls over sensitive and nonpublic documents it collects or exchanges with FSOC and OFR. Specifically, we recommended the Office of Information Technology (OIT) develop controls to prevent remote users from saving files accessed using Outlook Web Access to public computers.

Further, the Office of the Chairman should work with OIT to: (1) assign points of contact to serve as information owners, (2) develop a system to identify and track sensitive and nonpublic documents, and (3) devise procedures information owners should use to mark documents according to the sensitivity level, for all sensitive and nonpublic documents that are either provided to, or are received from FSOC or OFR.

### *Agency Expertise*

I see you are looking into allegations regarding the SEC's failure to follow established procedures for hiring or promoting senior-level staff positions to see if this is an agency-wide problem.

**Question:** As part of this report, or subsequent to it, have you thought about looking into whether the SEC has the right expertise within the agency?

**OIG Response:** Yes, as part of an ongoing audit we reviewed a sample 97 hiring decisions and promotions to determine, among other issues, whether the SEC followed the applicable regulations regarding eligibility for the positions in question.

**Question:** As in, do they understand the markets and products they regulate?

**OIG Response:** Employee qualifications, including understanding the markets and products they regulate, are important elements in achieving the SEC's mission. The objectives of the above referenced ongoing audit are to examine whether the SEC's Office of Human Resources (OHR) (1) adheres to applicable federal statutes and regulations and has adequate policies and procedures covering senior level vacancies in the competitive service, excepted service, and for senior officers; (2) ensures the SEC's hiring and promotion practices are carried out in a fair and consistent manner and in accordance with applicable federal statutes, regulations and OHR policy requirements; (3) communicates its hiring authority, decisions, and changes to the appropriate personnel; (4) ensures hiring and promotion decisions are documented in accordance with applicable federal statutes and regulations; and (5) takes action in accordance with applicable federal statutes and regulations and OHR policy pertaining to improper hiring or promotions. Additionally, we will keep concerns regarding agency expertise in mind while continuing our work.

*Waste within Trading and Markets*

I was disappointed to hear of the waste within the Division of Trading and Markets with regard to their procurement of unnecessary computer equipment and software. I understand you are currently completing a follow-up to review management's response to your office's recommendations.

**Question:** Can you tell us whether reforms have been fully implemented within the Trading and Markets Division?

**OIG Response:** Yes, immediately upon affirming that SEC staff had taken unencrypted laptops on inspections of SROs, clearing agencies, and exchanges, our office notified the SEC's Office of General Counsel and SEC Chairman Schapiro's office of this information. In response, the SEC took several remedial steps to ensure the immediate safety of SRO, clearing agency, and exchange data. OIT informed the OIG that it had taken possession of 28 lab laptops and contracted with an outside forensics team to conduct forensic testing on several select laptops to determine if a breach of SRO, clearing agency, or exchange data had occurred.

Our office has completed its investigation of an anonymous complaint alleging mismanagement of a security lab in the Division of Trading and Markets, Report No. OIG-557. In the investigation, we found that although the lab's budget was vetted by a project review board and the actual equipment and software purchases were submitted through OIT, neither the review board nor OIT knew enough about the lab, its mission, or the items it was purchasing to adequately judge whether the money was being effectively spent. Further, the OIG found that the lab continued to spend money on technology despite not having the staff to implement the technology it was buying.

Accordingly, several policy changes were implemented within the lab in order to ensure the security of lab equipment. In a memorandum dated May 29, 2012, the SEC CISO explained that "all information received from our markets and clearing organizations is corporate sensitive information that has been classified by the Division as non-public information and should be protected against both unauthorized and accidental disclosure."

Question: Are your recommendations applicable agency-wide?

**OIG Response:** Yes, our recommendations are made to the agency and are then directed to the Division or Office responsible for the program for which the recommendations are made.

**Question:** Have you discussed implementing more internal controls on this kind of procurement within other divisions at SEC?

**OIG Response:** Yes, we also provided a copy of the report to the OIG Office of Audits for consideration of conducting follow-up audits of the lab and, more broadly, of the purchase of information technology equipment throughout the SEC, to ensure that proper controls are in

place to prevent waste and potential data breaches in the future. Additionally, we consider previous audit work, among other things, in planning our future audits.

### **Questions for the Record Submitted by Congressman Tom Graves**

#### ***Misuse of funds allocated for the SEC's Trading and Markets division***

**Question:** How could the SEC allow \$1 million of laptops to be purchased for staff that did not exist?

**OIG Response:** In our investigation, we found that the lab staff spent over a million dollars on computer equipment and software with little oversight or planning and that much, but not all, of the equipment and software purchased was unneeded or never used in the inspection program. This was accomplished in part, because two members of the lab staff admitted to misrepresenting in contracting documents that the lab needed brand specific laptops because the entities they were inspecting were commonly using the same brand's laptops and the tablets were needed for "war-driving," a method for identifying wireless access points. However, the OIG found that those products were not commonly used at the entities the lab staff inspected and that tablets cannot be used for war-driving because they have no external port to connect an antenna.

**Question:** Do you feel that merely firing two employees was a sufficient response to gross negligence provided by taxpayer dollars?

**OIG Response:** In conducting our investigations, we gather evidence to indicate whether the actions or behavior of individuals are in violation of law and standards of ethical behavior. As fact finders we strive to remain independent of management decisions and functions, such as disciplinary actions. Therefore, this office cannot opine on the sufficiency of individual disciplinary actions. However, in the instant matter, two SEC employees were placed on paid, non-duty status pending completion of the aforementioned investigation. Both employees resigned shortly before the report was issued.

**Question:** What actions are being taken by your office to ensure that funding allocated to the Trading and Markets division is used to effectively serve the SEC mission to protect investors, maintain fair, orderly, and efficient markets, and facilitate capital formation?

**OIG Response:** Our office will continue to perform independent and objective audits and investigations of procurements to ensure that expenditures of funds by the SEC are made for their intended purposes and comply with requisite laws and regulations.

#### ***SEC Budget Request***

**Question:** What is the current status of the SEC budget request?

**OIG Response:** The submission of the SEC-wide budget request is not a programmatic function managed by the OIG. However, according to the SEC's Office of Legislative and Intergovernmental Affairs the SEC's budget request will be submitted on April 10, 2013.

### ***BCG Recommendation for reforming the SEC***

**Question:** Why have SEC Chairmen Schapiro and Walter failed to fully implement all of the recommendations contained in the Boston Consulting Group's (BCG) report issued pursuant to Dodd-Frank Section 967?

**OIG Response:** Our office does not have an independent body of work to draw from in order to opine on the issues associated with full implementation of BCG's recommendations. However, we note that the SEC, in its three status updates in response to the BCG recommendations, represents that a majority of the recommendations been implemented.

**Question** The BCG made recommendations for streamlining and improving the SEC, but few of their recommendations have been implemented. What was the purpose of the study, on which the SEC spent almost \$4.85 million?

**OIG Response:** The study was conducted to satisfy the requirements of Section 967 of the Dodd-Frank Wall Street Reform and Consumer Protection Act that directed the SEC to engage an independent consultant to examine the internal operations, structure, and the need for reform of the SEC.

**Question:** What can you say to assure us that you will be streamlining/heeding the recommendations from the study going forward?

**OIG Response:** The implementations of BCG's recommendations are not a programmatic function managed by the OIG. However, the OIG notes that the BCG report, issued March 10, 2011 provided 20 initiatives designed to increase the SEC's efficiency and effectiveness. As stated in the SEC's Third Report in the Implementation of SEC Organizational Reform Recommendations, the SEC established the Mission Advanced Program (MAP), which provided the framework for evaluating and implementing the changes. The BCG approaches were assigned to working groups composed of Division and Office executives and staff. As further stated in the report, 15 of the 20 initiatives examined have been completed and the implementation phase is complete or in process for each.

### ***Share Ownership Disclosure***

As you may know, there have been proposals from corporate lawyers and private sector market participants to change rules relating to the timing of share ownership disclosure. These proposals have proven controversial among a wide coalition of union pension funds, mutual funds, index funds, traditional asset managers and alternative asset managers (see letter from Congressman Garrett attached). These institutional shareholders have urged to Commission to undertake a deep review of the issue before suggesting rules changes as those changes may

impair effective shareholder oversight and corporate governance. When asked whether an economic costs/benefit review process would precede any concept release or other proposals in this area former-Chairman Schapiro suggested that the SEC's Division of Risk, Strategy, and Financial Innovation (known as RiskFin) would be consulted in advance for a thorough cost benefit analysis. In its outlook for 2013, the SEC published that it will prepare a concept release for the Commission's consideration on approaches to changing reporting requirements for large holders of stock--see page 31 <http://www.sec.gov/about/secpar/secapr2012.pdf>. Mr. Hoecker, in its outlook for 2013, the SEC published that it will prepare a concept release for the Commission's consideration on approaches to changing reporting requirements for large holders of stock.

**Question:** Can you confirm whether the Division of RiskFin has been included or will be included in this process before anything is published?

**OIG Response:** Our office does not have an independent body of work from which to draw from to establish to what extent a cost-benefit analysis was performed by the Division of RiskFin in preparing the aforementioned rulemaking. However, as our audit of the SEC's rulemaking activities continues, we will keep these concerns in mind and report any related information we find.

### **SEC Funding**

**Question:** As the IG, what do you see as the impacts of uncertain funding for the SEC? Is it hurting the effectiveness of the Agency?

**OIG Response:** Our office does not have an independent body of work from which to draw from to assess the impact of various and uncertain levels of funding for the SEC. However, as noted in the BCG report, the complexities of the SEC's role has increased as a result of both expanded legislated responsibilities under Dodd-Frank and the evolution of securities markets, and that despite the material increases in responsibility driven by Dodd-Frank and the attendant increase in workload, the SEC's resources have not grown in proportion.

**Question:** Do you have a view on self-funding, like that available to other key financial market regulators, like the Federal Reserve, FINRA, and the NYSE?

**OIG Response:** Our office does not have an independent body of work from which to draw from to opine on the impact of self-funding for the SEC. However, we note that the BCG found that, "In contrast [to self-funded regulators], other regulators have increased resourcing to respond to the crises or to changing regulatory environments."

### **Questions for the Record Submitted by Congressman Kevin Yoder**

#### ***SEC Efficiency***

In your testimony, you note that it is the OIG's mission to promote the efficiency and effectiveness of the SEC's programs and operations (p. 2). I am concerned that the SEC is not

being efficient or effective in its rulemaking under Dodd-Frank and the J.O.B.S. Act because it is focusing too many of its limited resources on rulemakings that are not required by Congress. For example, the SEC has spent more time working on regulating Money Market Funds (which are not a part of Dodd-Frank or the Jobs act) than it has on congressionally mandated rulemakings, even after it already implemented significant new regulations to MMFs in 2010. The SEC's lack of focus has caused the SEC to miss several statutory deadlines.

**Question:** Given the tight resources in our current budgetary environment, will the IG's office monitor the SEC's sequencing of rulemaking to ensure that the SEC is being efficient with its resources and not spreading itself too thin?

**OIG Response:** Our office does not have an independent body of work specific to the sequencing of rulemaking, such as discretionary rulemakings over Dodd-Frank or JOBS Acts required rulemakings. However, as our audit of the SEC's application of cost-benefit analysis during the SEC's rulemakings continues, we will ensure information found to be responsive to this question is reported and also considered in our planning process for future audits. Additionally, as agreed during the March 12, 2013 hearing, our office will review the impetus behind the SEC's Division of Corporate Finance's decision to post an agenda item with the Office of Information and Regulatory Affairs, Executive Office of the President that stated, "The Division is considering whether to recommend that the Commission issue a proposed rule to require that public companies provide disclosure to shareholders regarding the use of corporate resources for political activities."

**Question:** Will the IG analyze and report back to congress on how effectively it is prioritizing congressional mandates vs. rules not mandated by congress, and how well the SEC is meeting congressional deadlines?

**OIG Response:** As the OIG continues to rebuild its operational capabilities described below, we will strive to simultaneously meet all mandatory and Congressional requested work.

### ***Inspector General Priorities***

**Question:** As the new Inspector General, what are your priorities for the upcoming year? For your tenure?

**OIG Response:** On February 11, 2013, I began my tenure as the Inspector General of the SEC. The office I encountered has talented staff that had been without a permanent leader for over one year. The key senior leadership positions of Deputy Inspector General and the Assistant Inspector General for Investigations were vacant, as well as six staff positions. Unfortunately, the office is also faced with a pending litigation brought by a former employee requiring every staff member in the office to be responsive to discovery requests and, most likely, depositions. This is truly a situation where OIG cannot successfully carry out its mission.

My top priorities for this year are to:

- Complete the two audit reports on cost-benefit analysis requested by the House Government Oversight Committee.
- Complete other statutorily required work.
- Hire the two leaders (Deputy Inspector General and Assistant Inspector General for Investigations).
- Fill the remaining vacant positions.
- Continue to investigate complaints of misconduct reported to OIG.
- Complete the process of rebuilding the OIG.
- Determine what audit work can be done for the remaining fiscal year.
- Complete an audit plan for next fiscal year.
- Be as responsive to future Congressional requests for information.

### *Cyber Security*

The SEC has been repeatedly criticized for weaknesses in its cyber-security. As the agency is privy to large amounts of proprietary business data, the agency is a prime target for commercial espionage.

Question: Will you look at how the agency will protect information?

**OIG Response:** We conduct periodic assessments and reviews of the Commission's controls for protecting its information. Additionally, we assess and review information security controls based on our Annual Audit Plan. For example, during 2012 to 2013, we assessed the SEC's system and network logs, reviewed the SEC's controls over the handling of sensitive/nonpublic information collected and exchanged with the Financial Stability Oversight Council, its member agencies, and the Office of Financial Research; and reviewed the SEC's system certification and accreditation process. In each of these assessment/reviews, we made recommendations to improve the Commission's ability to protect its information.

Annually, as required by Title III of the E-Government Act of 2002, the OIG performs reviews of the Commission's information security program. This assessment includes but is not limited to the requirements set forth by the Department of Homeland Security and Office of Management and Budget. We plan to continue to conduct these independent reviews annually.

Going forward, we plan to continue our efforts to assess and review how the Commission will protect its information. In addition to meeting our annual FISMA requirement, we plan to conduct assessments and reviews of information security components.

Question: What steps is the agency taking to improve cyber-security?

**OIG Response:** The SEC's Office of Information of Technology (OIT) has taken steps to improve cyber-security within the Commission by implementing recommendations identified by our office, as well as the U.S. General Accountability Office. One of those steps taken was to implement the Plan of Action and Milestones as identified during OIT's assessment of its



security controls. In addition, OIT indicates it currently has several countermeasures in place to protect the Commissions information such as Anti-virus devices, firewalls, intrusion detection devices, encryption, content filtering, and trusted internet connections. OIT further indicates it is taking steps to improve the agency's information security program, including cyber-security, by implementing enterprise governance, risk, and compliance; policies and procedures consistent with NIST and other Federal guidelines; improved security awareness training program; threat assessment and modeling; data loss prevention, and web security assessment. While the Commission has these measures in place, improvements are still needed. Reviews and assessment by the OIG office will assist in identifying improvements to the Commission's cyber-security controls.

### ***Pending Cases***

The agency has had several scandals over the past several years including accessing obscene material on computers, entering into leases without having appropriated funds and losing laptops at a hackers convention.

**Question:** What is the status of these cases?

**OIG Response:** All investigations into these matters have been completed and the reports have been issued.

**Question:** What managerial changes are needed to prevent these problems from reoccurring?

**OIG Response:** Based on our work in the requisite subject matters, we reported that the SEC has improved its internet monitoring capabilities to prevent access to inappropriate materials from SEC equipment; has transferred its leasing authority to GSA; and, there was no evidence that laptops or any IT equipment was lost or stolen at the aforementioned convention. Additionally, full forensic analysis completed on the subject equipment revealed no evidence of compromises.

Although improvements in these areas have been made, as our work across the SEC continues to identify those areas most in need of improvement, we will continue to make recommendations to bolster the SEC programs and operations.



TUESDAY, MAY 7, 2013.

**U.S. SECURITIES AND EXCHANGE COMMISSION**

**WITNESS**

**MARY JO WHITE, CHAIRMAN, U.S. SECURITIES AND EXCHANGE COMMISSION**

Mr. CRENSHAW. Well, it is 2 o'clock so I will ask the hearing to come to order. I just want to make everyone aware that at about 2:10 there will be a vote called, but I think we will have time to get started. So I want to just begin by welcoming our witness, SEC Chairman Mary Jo White. Thank you for being here today and congratulations on your confirmation.

The SEC has the unique and critical task of protecting investors, maintaining fair and efficient markets, and encouraging capital formation. These are things that touch the lives of many and have a profound and far-reaching effect on our domestic as well as our global economy.

Since 2001, Congress has provided the SEC with additional regulatory tools and has drastically increased the Commission's annual appropriation, and yet the agency has missed major investor frauds like Madoff and Stanford, as well as several embarrassing management lapses such as purchasing unneeded space, destroying investigative documents and repeating material weaknesses in the SEC's own financial statements, just to name a few.

So while the SEC has made some progress in addressing these lapses, I believe that some of these problems are symptomatic of the fundamental problems within the SEC's organization and structure, and this committee is not inclined to throw more money at the SEC until these fundamental problems are addressed in a meaningful and comprehensive way.

The fiscal year 2014 request proposes another substantial increase of 27 percent over fiscal year 2012 and a 33 percent increase over the sequester level. Just because the SEC is funded by fees does not excuse the Commission from rigorously managing the funding it has and certainly doesn't discharge this subcommittee from providing serious oversight.

So I look forward to hearing how the Commission under new leadership intends to provide investors with confidence in the markets, take strong enforcement actions against individuals committing fraud, help facilitate access to capital for American businesses, and to effectively use and manage the resources provided to you to run your operations.

The SEC is facing many challenges, including finishing up the Dodd-Frank and JOBS Act rulemakings, modernizing the technology systems and being thoughtful in tackling these challenges. I think there are a lot of rulemakings still left to be completed, and

I hope that you will take a measured and thoughtful attitude toward that.

Chairman White, we recognize that you have a very difficult job. We know that you and your staff are working hard and we appreciate your efforts. As the newly installed chair of this agency, you have the opportunity to make meaningful reforms and significantly impact the management and efficacy of the Commission. We appreciate your willingness to take this challenging position, and your experience, both as a prosecutor and in the private sector, should be very useful to you as you work to improve the Commission and the functioning of our securities markets. We look forward to working with you in partnership with you on these challenges, and we look forward to your testimony.

Now I would like to recognize Mr. Serrano, the ranking member, for any opening remarks he might make.

Mr. SERRANO. Thank you, Mr. Chairman. I also join you in welcoming the new chair of the Securities and Exchange Commission, Mary Jo White, before the subcommittee. I must admit publicly that I was pleased when President Obama announced his nomination of Chairman White as the new head of the SEC. The SEC is our cop on the beat for Wall Street, and its enforcement and oversight duties are of the utmost importance in preventing another financial meltdown. I am heartened that we now have a former U.S. Attorney leading the agency because I believe you understand the importance of these core missions and ensuring the safety of our financial markets, preventing abuse of investors and in deterring future misconduct.

Unfortunately, we cannot discuss the fiscal year 2014 budget request without talking about the elephant in the room, and I am not referring about my Republican colleague, Congress' failure to come up with a comprehensive solution to sequestration. For the SEC the sequester has resulted in a cut of \$108 million in fiscal year 2013. Although the SEC has been able to avoid furloughs and layoffs, those cuts have come at the expense of your core roles, oversight of our financial markets, enforcement against those who engage in wrongdoing and implementation of the mandates that Congress has given to the agency.

Based on the Ryan budget passed by the House of Representatives in all likelihood the agency's budget is going to be reduced even further in any legislation proposed by this subcommittee. I hope you can discuss the impact of the cuts that you have already endured as well as your views on further potential cuts to the SEC. I feel confident that we share a similar opinion on this subject that it is an unwise investment choice to reduce funding for an agency that plays a key role in ensuring a fair playing field in our financial markets.

Your agency's budget request of \$1.674 billion in fiscal year 2014 seeks to invest in efforts that will improve the operation of your agency. Moreover, the budget request will help continue the implementation of Dodd-Frank financial reform and will ensure that the agency has the resources needed to address your expanded oversight role. Your testimony does a pervasive job of laying out the case for the necessity of these increases, and I hope that my colleagues will take this request to heart.

Although you have only been on the job a short time, I look forward to getting your thoughts on the SEC's current and future challenges. Once again we welcome you.

Mr. Chairman, the elephant comment was about the GOP. There might be some young folks in the audience that didn't get that.

Mr. CRENSHAW. I didn't get it. Anyway, thank you, Mr. Serrano.

I will now recognize Chairman White for an opening statement and let you know your written statement will be included in the record. So, please, the floor is yours.

Ms. WHITE. Thank you very much. Chairman Crenshaw, Ranking Member Serrano, and members of the subcommittee, I too look forward to working with all of you as we go forward and thank you for this opportunity to testify in support of the President's fiscal year 2014 budget request for the Securities and Exchange Commission and to discuss how the SEC would effectively use the \$1.674 billion requested to support additional staff, technology and training needed to fulfill our mission.

First, to acknowledge Public Service Recognition Week, I would like to express my appreciation to all public employees for the work they do every day and particularly to the staff of the SEC. Although I have been at the agency less than a month, I have been struck by their incredible commitment, talent and expertise. Our markets remain the envy of the world in large part because of their work writing effective regulations, ensuring comprehensive disclosure and vigorously enforcing the securities laws.

In addition to enforcing those laws, the SEC currently is charged with overseeing 25,000 market participants and reviewing disclosures of over 9,000 reporting companies, a range of responsibilities that has increased considerably with the passage of the Dodd-Frank and JOBS Acts. With the resources provided by Congress in recent years, the SEC has bolstered its examination and enforcement functions, enhanced its technology and made important internal improvements. Much more, however, remains to be accomplished.

The SEC's current funding level presents significant challenges as we seek to keep pace with the growing size and complexity of the securities markets. If enacted, our request would permit us to add approximately 676 new positions to improve core operations and implement the agency's new responsibilities. While our funding is fully offset by securities transaction fees and thus will not impact the deficit, we fully understand we must seek to use appropriated funds in the most efficient and effective way possible.

More specifically, our budget request would allow us to expand oversight of investment advisers. The number of registered advisers has increased by more than 40 percent over the last decade while their assets under management have more than doubled to over \$50 trillion. Yet during fiscal year 2012, the SEC was able to examine only about 8 percent of registered advisers and over 40 percent remain to be examined for the first time.

Although we have at the agency employed more risk-based analytics to target advisers selected for review and those advisers examined in fiscal year 2012 represented 20 percent of the assets under management, significant additional coverage is essential.

This request would permit us to hire 250 additional examiners to increase the percentage of advisers examined each year.

Our request would also permit us to bolster the enforcement program and continue to send a strong message to would-be wrongdoers that misconduct will be swiftly and aggressively punished. We would focus our enforcement hiring on increased expertise in the securities industry, trial attorneys, forensic accountants and staff for the offices of the whistleblower and market intelligence.

Our request would also permit 45 additional positions in the Division of Risk Strategy and Financial Innovation, a roughly 45 percent increase in the size of this essential function. These positions would be used primarily for additional economists to perform economic analyses in support of the Commission's rulemaking and other activities, including economists with expertise in analyzing high frequency trading data and market structure practices.

The Commission's regulatory responsibilities also have expanded with respect to security-based swap registrants. To avoid bottlenecks and unintended market disruptions, we need additional technical staff to process requests for rule interpretations, registrations, and required approvals or exemptions. New staff will also be needed to supervise registered security-based swap dealers and other market participants.

We are also requesting new positions for the Division of Corporation Finance to, among other things, review draft registration statements submitted by emerging growth companies under the JOBS Act and finalize remaining statutory rulemaking mandates. The additional positions also would allow enhanced review of regulations impacting small business capital formation.

The SEC's need to invest in technology cannot be overstated. While the SEC is rapidly modernizing our systems, significant investments are needed to properly oversee the markets and entities we regulate. Technology initiatives that would be funded under this request include improvements to our system for receiving tips, our IT security and our IT infrastructure.

In addition, we plan to use our statutorily created Reserve Fund to fund large, mission-critical technology projects, including our multiyear effort to overhaul the Edgar System and to construct the enterprise data warehouse which will create a central repository for SEC data and effect significant efficiencies in our ability to fulfill our mission.

We are also working to reduce costs wherever possible, and have achieved substantial technology-related cost savings in fiscal year 2012 of approximately \$12 million, including some initiatives that focused on more robust IT infrastructure, support contracts and savings in software maintenance contracts.

We also seek to increase our training budget to keep pace with the rapidly evolving markets in areas of new responsibility. Effective training is essential to maximizing the efficiency and expertise of our staff.

In conclusion, I appreciate your consideration of the President's budget request, and your support for the SEC's mission and its expanded responsibilities. It will allow us to better protect investors and facilitate capital formation, more effectively oversee the mar-

kets and entities we regulate and build upon the significant improvements the SEC has made to date.

Thank you very much for inviting me to be here. I would be happy to answer your questions.

[The statement of Ms. White follows:]

**Testimony before the  
Subcommittee on Financial Services and General Government  
Committee on Appropriations  
United States House of Representatives**

**by Chair Mary Jo White  
U.S. Securities and Exchange Commission**

**May 7, 2013**

Chairman Crenshaw, Ranking Member Serrano, and Members of the Subcommittee:

Thank you for the opportunity to testify today in support of the President's fiscal year (FY) 2014 budget request for the U.S. Securities and Exchange Commission (SEC).<sup>1</sup> I welcome the chance to discuss how the SEC would make effective use of the \$1.674 billion requested for the coming fiscal year and to explain why the agency needs the funding it is seeking to do the job it is required to do on behalf of investors and our capital markets.<sup>2</sup> As described in more detail below, the agency's funding request is critical to support the additional staff, technology, and training needed to fulfill our mission. Even though our funding mechanism is deficit-neutral, I recognize it is critical that we use appropriated funds in the most efficient and effective way possible as stewards of these resources.

As you know, the SEC has a broad, three-part mission: to protect investors, maintain fair, orderly, and efficient markets, and facilitate capital formation. Although I have been at the agency less than a month, two things were immediately apparent: first, the tremendous scope and

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<sup>1</sup> A copy of the SEC's FY2014 Budget Congressional Justification can be found on our website at <http://www.sec.gov/about/reports/secfy14congbudgetjust.pdf>.

<sup>2</sup> The views expressed in this testimony are those of the Chair of the Securities and Exchange Commission and do not necessarily represent the views of the President or the full Commission. In accordance with past practice, the budget justification of the agency was submitted by the Chair and was not voted on by the full Commission.



importance of that mission, and second, the exceptional level of commitment, talent, and expertise the agency's staff demonstrates each and every day on behalf of America's investors and markets. The U.S. markets are the envy of the world precisely because of the SEC's work effectively regulating the markets, requiring comprehensive disclosure, and vigorously enforcing the securities laws. I am honored to have the opportunity to lead the SEC in executing its mission.

Today, the SEC's jurisdiction and responsibilities have evolved to cover significant new aspects of the securities markets. As part of its core responsibilities, the SEC is charged with implementing and enforcing the federal securities laws, overseeing thousands of key market participants (over 25,000 entities currently),<sup>3</sup> and reviewing disclosures and financial statements of approximately 9,100 reporting companies. With the passage of the Dodd-Frank Wall Street Reform and Consumer Protection Act (Dodd-Frank Act) and the Jumpstart Our Business Startups Act (JOBS Act), the agency's importance and scope of responsibilities increased, with the Dodd-Frank Act giving the Commission significant additional responsibilities for over-the-counter derivatives, hedge fund and other private fund advisers, municipal advisors, and security-based swap clearing agencies, and the JOBS Act providing new private offering exemptions, including a new regime for crowdfunding offerings.

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<sup>3</sup> These participants include about 10,600 investment advisers, 9,700 mutual funds and exchange traded funds, 4,600 broker-dealers, and approximately 460 transfer agents. We also oversee 17 national securities exchanges, seven active registered clearing agencies, and 10 nationally recognized statistical rating organizations (NRSROs), as well as the Public Company Accounting Oversight Board (PCAOB), Financial Industry Regulatory Authority (FINRA), Municipal Securities Rulemaking Board (MSRB), the Securities Investor Protection Corporation (SIPC), and the Financial Accounting Standards Board (FASB).

In recent years, the agency has made significant strides forward to strengthen its oversight over markets that are so critical to the savings of American families and to the growth potential of American businesses. With the help of the resources provided by Congress in recent years, the SEC has bolstered its examination and enforcement functions, improved its capacity to assess risks, and enhanced its technology. It also has made a number of necessary and important internal improvements designed to maximize efficiencies and reform its operations. Much more, however, remains to be accomplished.

The SEC's current level of resources still presents significant challenges as we seek to keep pace with the growing size and complexity of the securities markets and fulfill our broad mandates and responsibilities. The FY 2014 budget request – all of which would be fully offset by matching collections of fees on securities transactions and thus will not increase the Federal budget deficit – seeks to address these challenges directly, to better position the agency to provide the kind of market oversight that the public expects and deserves.

Before delving into the details of our funding needs for 2014, I would like to briefly highlight a few key areas that I believe should be our top priorities and that have been important drivers for our budget request.

### **Key Priorities**

First, the SEC must complete, swiftly and thoughtfully, the rulemaking mandates contained in the Dodd-Frank Act and JOBS Act. Of the more than 90 Dodd-Frank Act provisions that require SEC rulemaking, the SEC has proposed or adopted rules for over 80

percent of them, and also has finalized 17 of the more than 20 studies and reports that it was directed to complete. But there is still much Dodd-Frank Act work that remains. Similarly, the JOBS Act requires significant Commission rulemaking which has not yet been completed. To fulfill these legislative mandates expeditiously must be an immediate imperative for the Commission. In connection with those rules, I will continue the Commission's efforts to ensure that the SEC performs robust economic analysis, as rigorous economic analysis is important and should inform and help guide our decisions.

While the Commission, with its existing staff, is already far along in many of its statutorily mandated rulemakings, we need additional staff and investments in technology to successfully implement these mandates. For example, the FY 2014 budget request would enable the SEC to bring in more economists to perform economic and risk analyses to assist in all of our rulemaking decisions, as well as support new technology for a municipal advisor registration system. We also need additional resources to improve our ability to help our markets and participants transition to new rules and requirements. Market certainty is critical to its functioning, especially during periods of regulatory change. The FY 2014 request would allow us to hire additional staff with technical skills and experience to process and review on a timely basis requests for interpretations, registrations, and other required approvals. Additional resources also will be needed to help conduct risk-based supervision of newly registered entities such as security-based swaps dealers and major swap participants, which will be subject to registration and regulation by the agency.

Second, I am committed to further strengthening the core enforcement and examination functions of the SEC. Strong enforcement of the securities laws is necessary for investor confidence and is essential to the integrity of our financial markets. Successful enforcement actions result in sanctions that deter and punish wrongdoing and protect investors, both now and in the future. Similarly, our National Examination Program (NEP) is critical to improving compliance, preventing and detecting fraud, and monitoring market risks. As described in more detail below, the current level of resources is not sufficient to permit the SEC to examine regulated entities and enforce compliance with the securities laws in a way that investors deserve and expect.

Third, the SEC needs to be in a position to provide adequate oversight over today's highly complex and dispersed marketplace so that it can be wisely and optimally regulated, which means without undue cost and without undermining its vitality. There must be a sense of urgency brought to understanding more fully the impact on investors and the quality of our markets of high-frequency trading, complex trading algorithms, dark pools, and intricate new order types so that appropriate regulatory responses can be made. I know that many in Congress are also interested in this important area. The FY 2014 budget request would assist the SEC in making investments in much needed technology and expertise, not only helping us keep better pace with the markets we monitor and regulate, but also permitting us to see around corners and anticipate issues that may arise.

## **FY 2014 Request**

The SEC is requesting \$1.674 billion for FY 2014. If enacted, this request would permit us to add approximately 676 new staff positions, both to improve core operations and implement the agency's new responsibilities. While we understand that this request comes during a time of serious fiscal challenges, we have tried to be as targeted as we could in making these requests in the areas where the immediate deployment of resources is most critical.

The budget request would provide additional funding for the following key areas:

- expanding oversight of investment advisers and improving their regulation and compliance – a point at which investors are most at risk of being defrauded and harmed;
- bolstering enforcement – a primary function of the agency is to enforce the law and deter other would-be wrongdoers;
- economic and risk analysis to support rulemaking and oversight – critical to good and valid rulemaking;
- building oversight of derivatives and clearing agencies – significant new agency responsibilities to help safeguard against future financial crises;
- enhancing reviews of corporate disclosures – including supporting implementation of the JOBS Act;
- leveraging technology – to improve our ability to detect wrongdoing, streamline our operations, and tighten the security of our data; and
- enhancing training and development of SEC staff – to increase our staff expertise.

I would now like to describe each of these in more detail.

### **Expanding Oversight of Investment Advisers and Improving Their Regulation and Compliance**

During FY 2012, although the SEC continued to use and improve risk-based analysis to select examination candidates in its examination program, it was able to examine only about

eight percent of registered investment advisers. Over 40 percent of advisers have never been examined. The number of registered advisers has increased by more than 40 percent over the last decade, while the assets under management by these advisers have increased more than two-fold, more than \$50 trillion. In addition to this exponential growth in size, the industry is increasingly complex. This complexity includes: the use of new and sophisticated products, including derivatives and certain structured products; technologies that facilitate high-frequency and algorithmic trading; and complex “families” of financial services companies with integrated operations that include both broker-dealer and investment adviser affiliates. Although the agency has successfully focused its limited examination resources on those areas posing the greatest risk to investor assets, the SEC’s examination coverage continues to be insufficient in comparison with the rates achieved by other financial regulators and in the opinion of many third-party observers.

Therefore, under the FY 2014 request, one of the SEC’s top priorities is to hire 250 additional examiners to increase the proportion of advisers examined each year, the rate of first-time examinations, and the examination coverage of investment advisers and newly registered private fund advisers. This would be an important step in a multi-year effort to increase coverage by our examination program to meet our regulatory responsibilities to investors who increasingly turn to investment advisers for assistance navigating the securities markets and investing for retirement and family needs.

The NEP also would be able to add 60 positions to improve oversight and examination functions related to broker-dealers, clearing agencies, transfer agents, self-regulatory

organizations (SROs), and municipal advisors. In addition, 15 positions would be used to support other critical program initiatives such as enhancing global risk assessment and surveillance efforts and improving technology capabilities. These positions are vital as the agency continues to strive to adapt to the rapid change and increasing complexity of the markets it regulates and its increased examination responsibilities with regard to clearing agencies, securities-based swap market participants, and municipal advisors.

### **Bolstering Enforcement**

The ability to identify and bring timely, high-quality enforcement actions when violations of the federal securities laws occur is integral to the SEC's core mission. The SEC must enhance its enforcement function not only to send strong messages to wrongdoers that misconduct will be swiftly and aggressively addressed, but also to adapt for the highly automated, high-speed, and high-volume markets of today and tomorrow. Under this budget request, we would be able to further refine our analysis of tips and leverage incoming data to identify trends of possible misconduct across product, sector, or geographic areas. We also would engage additional industry experts and proactive data analytics to better target industry practices that may harm investors. For example, we have developed certain algorithms to mine publicly available hedge fund performance data to identify aberrational performance returns that could be indicative of conduct warranting further investigation. With additional front line investigative attorney, trial attorney, and forensic accountant resources, we would further bolster our core work of pursuing potential securities laws violations identified from these and other sources. The Division of Enforcement would focus its hiring of 131 staff on increased expertise in the securities industry and new product areas, trial attorneys, and forensic accountants, as well as staff for the Office of

Market Intelligence, the Office of the Whistleblower, and the SEC's collections and distributions functions.

### **Economic and Risk Analysis to Support Rulemaking and Oversight**

For FY 2014, the SEC requests funding to add 45 positions in the Division of Risk, Strategy and Financial Innovation (RSFI), a roughly 45 percent increase in the size of this essential function. These positions would be used primarily for additional financial economists to perform economic analyses and research in support of the Commission's activities. Specifically, RSFI would seek economists with expertise in analyzing high frequency trading data and market structure and practices, executive compensation and related areas of corporate governance, and credit-default swaps in support of Dodd-Frank Act required rulemakings. RSFI also plans to hire operations research analysts with backgrounds in mathematics, statistics or econometrics to expand the development and delivery of risk metrics and analytics to inform risk assessment in examinations and investigations, rulemaking, and economic analysis.

### **Building Oversight of Derivatives and Clearing Agencies**

The Commission's regulatory responsibilities have been significantly expanded with the addition of new categories of registered entities (including security-based swap execution facilities, security-based swap data repositories, security-based swap dealers, and major security-based swap participants); the required regulatory reporting and public dissemination of security-based swap data; and the mandatory clearing of security-based swaps. To avoid bottlenecks and unintended market disruptions as the new requirements become operational over the next two years, the agency will need additional staff going forward with technical skills and experience to



process and review on a timely basis the requests for rule interpretations, registration, or required approvals. New staff also will be needed to supervise registered security-based swap dealers and participants, and to use newly-available data to identify excessive risks or other threats to security-based swap markets and investors.

In addition, the agency intends to focus on further enhancing its oversight of clearing agencies, including clearing agencies expected to register with the Commission in the near future. Currently, six clearing agencies have been designated systemically important by the Financial Stability Oversight Council (FSOC) and, of the six, the SEC is the supervisory agency for four. This has been accompanied by a materially higher level of work, including, for example, an annual exam requirement for the clearing agencies for which we are the supervisory agency and enhanced coordination with other agencies for proposed changes and supervision activities. We also anticipate additional work associated with Commission rules relating to clearing of security-based swaps, as the requirements are new and the relevant clearing agencies are new agency registrants.

Currently, the average transaction volume cleared and settled by the seven active registered clearing agencies is approximately \$6.6 trillion a day. Notwithstanding this tremendous volume, the SEC currently has on staff 14 examiners devoted to examining registered clearing agencies, with only a limited on-site presence existing in four of the seven. Additionally, the SEC has about a dozen other staff focused on the monitoring and evaluation of risk management systems used by the existing clearing agencies, and will need to expand these efforts to address the expected increase in the number of clearing agencies and rule filings

raising risk management issues. Without these additional resources, the mismatch between the amount of regulated clearing activity and staffing will be exacerbated both by the additional clearing agencies that are expected to register with the SEC as a result of security-based swap activities and the expanded oversight required due to clearing agencies' designations as systemically important by the FSOC. Accordingly, the FY 2014 budget request seeks to add 25 positions in the Division of Trading and Markets and in the NEP to support these functions.

#### **Enhancing Reviews of Corporate Disclosures, Including Supporting Implementation of the JOBS Act**

For FY 2014, the SEC requests 25 new positions for the Division of Corporation Finance. These positions would permit us to hire additional attorneys and accountants to continue to enhance the Division's reviews of large companies, review draft registration statements submitted by emerging growth companies under the JOBS Act, prepare and finalize the remaining rules and projects to implement the Dodd-Frank Act and the JOBS Act, and respond to requests for interpretive guidance, including with respect to new rules. Further, the additional positions would allow the Division to enhance its review of SEC rules and regulations impacting small business capital formation and better evaluate trends in increasingly complex offerings.

#### **Leveraging Technology**

Beyond the need to increase the number of experts dedicated to overseeing the securities industry, it also is critically important to continue leveraging technology to streamline operations and increase the effectiveness of the agency's programs. While the SEC has made significant progress over the past few years in modernizing our technology systems, the agency must continue to make significant investments if it is to properly oversee the markets and entities it

regulates. The FY 2014 budget request would add \$56 million for technology to support a number of key Information Technology (IT) initiatives, including enhancements to the system for receiving tips, complaints, and referrals (TCR), improvements to IT security, and infrastructure upgrades to achieve efficiencies in business operations and reduce long-term costs.

The SEC plans to enhance its TCR system by building an interface to the agency's exam and case management systems, adding intake and routing functionality for referrals from the self-regulatory organizations (SROs), and expanding internal reporting to SEC management on the tracking, investigation, and disposition of TCRs. Additionally, the agency plans to develop a component of the TCR system that will automatically triage incoming tips so they can quickly be flagged for additional follow-up.

The agency also seeks to make a significant investment in its information security program to deploy a new set of security tools and develop and train staff to monitor, respond to, and remediate threats. Additionally, the SEC is requesting resources to implement infrastructure upgrades that will achieve efficiencies in business operations and reduce long-term costs. For example, the agency plans a number of initiatives to automate business processes and share data across the agency, to improve collaboration and content management across the agency, and continue strategic replacement of existing hardware and software to hold down maintenance costs.

While the need for resources is significant, we also realize and appreciate the imperative to identify ways to reduce costs wherever possible, so we can dedicate more funds to fulfilling

our mission. The SEC has made important strides forward in this regard, identifying and realizing substantial savings and operational efficiencies in recent years. For example, in the technology areas, agency initiatives have resulted in more robust IT infrastructure support contracts, savings in software maintenance and support contracts, upgrades to data storage systems, and reductions in remote connectivity and network costs. Together these steps yielded cost savings of approximately \$12 million in FY 2012, and continued savings are expected in FY 2013 and beyond.

The SEC's savings initiatives are expected to continue into FY 2014, as the agency is working to identify and implement new technologies and business process improvements that will offer increased performance with reduced operational costs.

#### **SEC Reserve Fund**

In FY 2014, the SEC plans to use \$50 million from the SEC Reserve Fund, established by statute, to fund large, multi-year, mission-critical technology projects. As required by statute, we will continue to notify this Subcommittee within ten days of each obligation from the Reserve Fund. Among other projects, the agency would continue its multi-year effort to overhaul the Electronic Data Gathering, Analysis and Retrieval (EDGAR) system to create a new, modernized system that will meet Commission requirements for real-time system updates, reduce filer burden by providing simplified search and filing options based on filer experience (i.e., professional or novice), improve data capture by moving to structured formats for various SEC forms, and reduce the long term costs of operating and maintaining the system.

In addition, we plan to use the SEC Reserve Fund for the construction and enhancement of the Enterprise Data Warehouse (EDW). The EDW is a critical step in combining currently disparate sources of data from EDGAR filings, exam reports, investigations, external vendors, and many other sources. An organized central data repository will allow enhanced analytical capabilities, predictive modeling, and strengthened governance of data controls and quality standards.

We also plan to use the SEC Reserve Fund toward the development of the capability to intake, store and analyze data from the upcoming Consolidated Audit Trail (CAT) that the Commission has mandated the SROs create to increase the data available to regulators. A CAT repository would enable the SEC to intake CAT data and store it in the EDW, as well as to develop analytical tools and a single software platform that will allow the SEC to identify patterns, trends, and anomalies in the CAT data. The tools and platform will allow seamless searches of data sets to examine activity to reveal suspicious behavior in securities-related activities and quickly trace the origin.

### **Enhancing Training and Development of SEC Staff**

The SEC's hardworking staff is the most important component of the agency's successes. The FY 2014 request includes a significant increase in the SEC's total training budget to deepen expertise and skills, in order to keep pace with the rapidly evolving nature of the markets and areas of new responsibility. The planned investment principally supports training and development for employees directly involved in examinations, investigations, fraud detection, litigation, and other core mission responsibilities of the SEC. The training will consist of

specialized in-depth training concerning new trends in the securities industry and changing market conditions, the impact of the current market structure on compliance and trading activities, and analytics and forensics using market data. The resources requested in the FY 2014 budget would bring the SEC's level of training investment more on par with other Federal financial regulatory agencies.

**Conclusion**

I very much appreciate your consideration of the President's FY 2014 budget request. Your support for the SEC's expansive and vital mission will allow us to better protect investors and facilitate capital formation, more effectively oversee the markets and entities we regulate, and build upon the significant improvements we have made to date.

Thank you for inviting me to be here today. I would be happy to answer your questions.

## **SEC Biography: Chairman Mary Jo White**



Mary Jo White was sworn in as the 31st Chair of the SEC on April 10, 2013. She was nominated to be SEC Chair by President Barack Obama on Feb. 7, 2013, and confirmed by the U.S. Senate on April 8.

Chairman White arrived at the SEC with decades of experience as a federal prosecutor and securities lawyer. As the U.S. Attorney for the Southern District of New York from 1993 to 2002, she specialized in prosecuting complex securities and financial institution frauds and international terrorism cases. Under her leadership, the office earned convictions against the terrorists responsible for the 1993 bombing of the World Trade Center and the bombings of American embassies in Africa. She is the only woman to hold the top position in the 200-year-plus history of that office.

Prior to becoming the U.S. Attorney for the Southern District of New York, Chairman White served as the First Assistant U.S. Attorney and later Acting U.S. Attorney for the Eastern District of New York from 1990 to 1993. She previously served as an Assistant U.S. Attorney for the Southern District of New York from 1978 to 1981 and became Chief Appellate Attorney of the Criminal Division.

After leaving her U.S. Attorney post, Chairman White became chair of the litigation department at Debevoise & Plimpton in New York, where she led a team of more than 200 lawyers. Chairman White previously was a litigation partner at the firm from 1983 to 1990 and worked as an associate from 1976 to 1978.

Chairman White earned her undergraduate degree, Phi Beta Kappa, from William & Mary in 1970, and her master's degree in psychology from The New School for Social Research in 1971. She earned her law degree in 1974 at Columbia Law School, where she was an officer of the Law Review. She served as a law clerk to the Honorable Marvin E. Frankel of the U.S. District Court for the Southern District of New York.

Chairman White has won numerous awards in recognition of her outstanding work both as a prosecutor and a securities lawyer. The 2012 Chambers USA Women in Law Awards named her Regulatory Lawyer of the Year. Among other honors she has received are the Margaret Brent Women Lawyers of Achievement Award, the George W. Bush Award for Excellence in Counterterrorism, the Sandra Day O'Connor Award for Distinction in Public Service, and the "Women of Power and Influence Award" given by the National Organization for Women.

Chairman White is a fellow in the American College of Trial Lawyers and the International College of Trial Lawyers. She also has served as a director of The NASDAQ Stock Exchange and on its executive, audit, and policy committees. Chairman White is a member of the Council on Foreign Relations.

<http://www.sec.gov/about/commissioner/white.htm>

Mr. CRENSHAW. Well, thank you very much. They have just called a vote, but I think we will have time for the three members here to ask a question. We may take a recess. I think there are just two votes, maybe three. I will call on the members in terms of their seniority if they were here when the meeting started. Otherwise I will call on them when they get here and we will go back and forth from side to side.

Let me just start by saying you gave us a lot of requests and if you go back and look, since 2001 I think the SEC's budget has increased like 300 percent. As I mentioned in my opening statement, I think this year you are asking for a 27 percent increase, 33 if you do it over the sequester number, and actually in 2012 there was \$100 million more than the year before that. So as you can imagine, most agencies don't get this kind of increase every year, and I know that your budget is funded by fees and it doesn't come out of the general fund of the Treasury but we have to take our oversight role pretty seriously, so we have got to ask the questions.

How do you think that the average investor has benefited from these large funding increases and when is enough going to be enough? When do you expect that you can stop asking for these dramatically large increases every year? You touched on some of the things that you are doing to be more efficient. Please talk about that.

Ms. WHITE. Well, let me say first that we appreciate very much the funding support that we have gotten at the SEC over the years and seek that support again through this request. I guess one of the things that I have been most struck by since I became chair of the SEC, I should have known this well from the outside, but certainly you know it better from the inside once you are there, is just how vast and difficult and complex the responsibilities are of the SEC in terms of protecting investors, facilitating capital formation, and really safeguarding the integrity of our markets. Those markets are also changing as we speak every day, and we need to keep up with that complexity and that speed with the work that we do. So we are cognizant of these budgetary times, we are cognizant of our mission. We have had additional responsibilities added to that mission which was already a vast one.

So, we have tried to be as targeted as we can in these requests that we have made so it is a responsible request and we can do our job. Certainly I feel extremely strongly about being a faithful and strong steward for those moneys on behalf of the taxpayers. I think the agency has also certainly prior to my arrival made significant improvements to become more efficient and effective. I think others have testified before about a number of the restructurings in the enforcement and examination functions for example, and I think those have really yielded very good dividends. I expect to see more of that. I think those are extremely important functions for the SEC.

So it is our responsibility that we have to cover and discharge. It is also our responsibility to spend that money wisely and very effectively, and I am certainly committed to discharging that responsibility.

Mr. CRENSHAW. Thank you very much, and we look forward to your bringing a fresh approach as you go about your job.



Mr. Serrano.

Mr. SERRANO. Thank you, Mr. Chairman.

You came in the middle of an uncertain budget year between continuing resolution and sequestration. You have had quite a challenge to say the least. What impact have you seen from this uncertainty and from sequestration?

Ms. WHITE. I think what I have seen is a number of things not being able to be done that again I think are critical for the agency to do to fulfill its mission. Certainly our agency, and I am sure others as well, have anticipated the possibility of the sequestration. I think our folks have done an excellent job in planning for that so that we don't expect furloughs, but we certainly have had to defer hiring for some of our new functions, including oversight of OTC derivatives. We have had to suspend and will have to suspend certain of the critical IT initiatives that would help our examination and enforcement functions. And so it is quite an impediment to the agency. But I am glad to say that we are obviously trying to safeguard as much as we can for our core mission, but it is very much felt.

Mr. CRENSHAW. Mr. Graves has a question and then let's see where we are. Mr. Graves.

Mr. GRAVES. Thank you, Mr. Chairman.

Chairman White, I guess congratulations and welcome to your new post. I had a quick question in relation to portfolio margining. In your presentation you spoke a lot about enforcement and I think we all recognize that is a very, very important role that you have there, but as well in your statement you talk about maintaining fair, orderly and efficient markets. So as it relates to portfolio margining, and Dodd-Frank contained a provision that addressed this, and while there is a lot controversy with that piece of legislation, a lot I don't agree with, there are certain components that may be beneficial, and this was one of those, one of the few beneficial provisions, for exchanges that I guess where the portfolio margining would help with exchanges and with customers alike.

It is my understanding progress has been made recently with regard to permitting the holding of swaps, security-based swaps, in the same account, thus allowing customers to more efficiently use their capital.

Can you provide us with an update on the rulemaking activities with the SEC for this issue?

Ms. WHITE. I think I can, at least to the extent of my knowledge. Obviously a major objective of Dodd-Frank is to promote the clearing of OTC derivatives such as credit default swaps and others. ICE Clear Credit has agreed to clear such transactions, which is a very, very good thing. The SEC has issued an order providing relief in terms of some of the margin requirements looking towards permitting the portfolio margining that is essential and certainly beneficial to the dealers and the customers.

Essentially, some of those requirements became effective before all of the information was provided to the SEC in order to be able to approve the portfolio margining methodologies. So the SEC, I think in March of this year, actually issued letters to I think seven of the broker dealers to give them stopgap relief. There was some resistance to what the stopgap relief was, I think, in terms of high-

er margin requirements for the dealers. I could go into the rationale for that. But I think more importantly the bottom line is that since then the SEC has been very productive, I think, with constructive discussions with the dealers and with ICE to try to work out what would be an acceptable solution there.

Mr. GRAVES. So you all are still working on that?

Ms. WHITE. Yes, we are.

Mr. GRAVES. Okay, thank you.

Mr. CRENSHAW. Mr. Serrano.

Mr. SERRANO. Let me just ask you as a follow-up to that first question I asked, what are the long-term ramifications from your perspective on reducing oversight because of budget constraints? One of the big concerns that we have in all agencies is that the oversight that will be carried out or not carried out, and the IRS is collecting taxes and going after people who don't pay their taxes. In your case it is the oversight that we all need now more than ever. What do you think is the long-term effect?

Ms. WHITE. Of the oversight of the budget process?

Mr. SERRANO. Yes.

Ms. WHITE. If I understood your question. Look, I think, and I know there was a discussion before of self-funding for the SEC. It is deficit neutral funding. That doesn't change the oversight responsibilities of this subcommittee. It doesn't change the responsibilities of the SEC to effectively use those funds. I would hope that—

Mr. SERRANO. No, I am referring to the SEC's oversight of people who may be—

Ms. WHITE. I am sorry, I misunderstood your question.

Mr. SERRANO. I apologize.

Ms. WHITE. Clearly we need the resources to be able to do that, and we have gotten a number of new responsibilities. I think I cited we have 25,000 entities now that we oversee and we have more coming under the Dodd-Frank legislation in particular. So it is essential that we get the funding to be able to do that or we simply won't be able to perform our job.

Mr. SERRANO. Very briefly, Mr. Chairman, and this is in the record and can be seen, when I was chairman of this committee one of the surprises was having people from the SEC coming and basically tell us we don't need any more money. We have enough money. We later found out that what that meant was we have no intention of oversight and many can say that what happened on Wall Street happened in part because we weren't checking. And I don't mean the committee was not checking, the SEC was not checking.

Mr. CRENSHAW. Got you. Let me ask you one quick question, and then I think there are 334 people that haven't voted yet so I think we are in good shape.

Let me ask you, we are talking about rulemaking. The Inspector General has criticized the Commission in terms of the cost-benefit analysis, especially in those Dodd-Frank rulemakings. And you understand that these rules have a pretty big impact on the business world and that is important particularly when we have got a struggling economy. I notice in your budget request you are planning on

hiring some more economists and I would think that is a critical group for you to hire. So let me ask you about that.

Is this a pretty big priority of the Commission, to have some more economists? What role are they going to play in the rule-making process and are they going to be more active than they were in the past? It seems to me this is going to be a big step forward.

Ms. WHITE. I think there is no question that economic analysis, including cost-benefit analysis, is essential to our rulemaking function, and you rightly identify our economists as those that are intimately involved in that. The agency in March of last year actually issued guidance to enhance its economic analysis of its rulemaking.

We have actually gotten some positive comments about the progress in that area, both I think from the Chamber and also in a recent GAO report, more recent than the IG report that you cite, although the agency was quite responsive to all of the recommendations. I think it is essential going forward. There is a significant 45 percent increase adding 45 economists to our risk analysis section. We get them involved earlier in the process to judge the economic impact of a rule, whether there should be a rule, what the alternatives should be, and whether there should be one at all, as I mentioned. It is absolutely critical. I think the agency is totally committed to the robust economic analysis of its rule-making and I think it has enhanced itself over time in that analysis.

Mr. CRENSHAW. That is encouraging. I want to be sure, and I am sure you are aware, of how important that is in terms of the folks that you regulate. Now, some of those suggestions by the Inspector General, I guess you don't agree with everything, but some of the criticisms they had of you trying to implement those—

Ms. WHITE. I am not sure precisely which ones we are speaking of, but I know that the agency was responsive to a number of recommendations by the IG with respect to enhancing economic analysis. I think they have been responsive to recommendations coming from a number of corridors doing that. Certainly I would be responsive to recommendations that obviously I agreed with, but nevertheless it is a priority that our economic analysis continue to be robust, and if need be, enhanced as we go forward.

Mr. CRENSHAW. Great. Well, I think, Mr. Graves, do you want to ask a question? The clock has run out, but we are pretty fast. So we will go over there. I know some of the other members probably were going to wait until after votes to come, so it may be 15 or 20 minutes, but with your great understanding, I am going to recess the committee for a short period of time. Thank you.

[Recess.]

Mr. CRENSHAW. I will call the meeting back to order. Again, thank you for your patience. I think some members may be straggling in from time to time.

Let me just finish up one of the things that you and I were talking about, the rulemaking process and the economic impact and the cost-benefit analysis. One thought I had, I don't know if this is something you all do, kind of a look back at the rules and regulations that from time to time once a rule is promulgated that maybe after a year or two that you kind of review that rule, see if it ac-

complished what you wanted to accomplish, see if it cost what you thought it might cost. Is that something you all have thought about or would that be a good idea? I know everything has changed, as you say, and you got to look to the future, but would it be helpful to look back and see, make sure there aren't any unintended consequences, make sure that things are working out the way you had them planned?

Ms. WHITE. With respect to that, I think that we rely on a very robust post-comment period as well from the parties affected by the rules. It is not a formal notice and comment after you adopt the rule. Certainly you want to remain on top of the markets and the impacts of your rules. But I think primarily we rely on the input that we get from our own monitoring of the rules as well as comments we get from those affected.

But I think there was actually a GAO study in 2007 that suggested that actually prescribing a formal look back might not be as efficient as actually sort of receiving input from those affected every day. So we certainly are cognizant of that, but at least to my knowledge there is not a formal program to do that. But we certainly do monitor our rules and we are in constant dialogue with those we regulate.

Mr. CRENSHAW. I think that makes sense. I wasn't suggesting that some sort of official procedure take place, but it sounds to me like you are doing just that, when you promulgate the rules, and as you informally look back and see if they need a change or if they are working well. So I think that is good.

Let me call on Mr. Serrano.

Mr. Quigley wasn't here and he just got here. Why don't we do that, even though Mr. Serrano was here first.

Mr. QUIGLEY. Let Mr. Serrano go first.

Mr. CRENSHAW. Mr. Quigley insists that Mr. Serrano go first.

Mr. SERRANO. I have never been so loved. So the big issue that we always continue to discuss in Congress or at least among ourselves is, you know, can what happened in 2008 happen again and what role can the SEC play in making sure that it doesn't happen. And we come back to the point of can you do that without getting all the staff positions you need? We know that we are in a budget cutting situation and some folks think you cut right across the board, but all agencies, of course, are important, but this is the one that has to keep an eye on making sure that that which caused such a huge problem in our economy doesn't happen again. What can you tell us about that?

Ms. WHITE. Well, there is no question that obviously none of us want anything like that to happen again. I think I can say this as the relative newcomer as chair to the SEC, that there is also no question that the SEC is absolutely critical to seeing that it doesn't happen again, critical to our markets in general. And I also think we were given over 90 rulemakings under the Dodd-Frank Act designed to prevent that, frankly, by greater regulation.

So it is critical that the SEC be able to carry out those rules as well as those under the JOBS Act. Without the resources, it makes it very, very difficult. Then even once adopted, those rules have to be implemented, enforced, monitored. And we have new regulated

entities, registered entities coming on board all the time that are really quite resource intensive.

One of the effects of sequestration is that we are not as able to do as much as we would like to do to build for those new entities that we oversee, and it is critical that we be able to do so.

Mr. SERRANO. Briefly how many rules are we talking about and how many are in place or ready to go?

Ms. WHITE. The SEC under Dodd-Frank has adopted, or proposed about 80 percent of the rules under Dodd-Frank, but that doesn't mean all are adopted. So there are a lot that remain to be done, including the Volcker rule that there has been a lot of discussion about. Under the JOBS Acts those rulemakings remain to be done. And one of my highest immediate priorities, as I said at my confirmation hearing, is to get those congressionally mandated rules done as promptly as I can and as well as I can.

Mr. SERRANO. Thank you.

Mr. CRENSHAW. Mr. Bonner.

Mr. BONNER. Thank you, Mr. Chairman.

Madam Chair, I apologize for being late, so if I go into two questions that have already been covered you are happy to refer me to the record and I will be happy to go there and not ask you to repeat yourself.

The first one deals, and I know you have only been in your current position for a couple months, so thank you for your public service and your career of public service. But the first goes to the Stanford victims. And like many victims of Congress I have some in my district that I have met with and felt their frustration, felt their loss, felt their hopelessness that they were not being adequately looked after by their Federal Government they have paid taxes to all these years.

The SEC, as you know, recently launched a lawsuit against SIPC in the Federal District Court which it had pursued on behalf of the Stanford victims. They allege that the SEC, or at least the ones I have talked with in Alabama, failed to properly make their argument and specifically that they improperly agreed to SIPC's incorrect stipulations of a particular set of facts. The Stanford victims that I have met with over the years agree to SIPC's incorrect stipulations—I am sorry, they argue that the SEC had agreed to SIPC's stipulations, contrary to the fact that for many Stanford victims these stipulations were simply not accurate.

So the constituents I have, in particular Craig and Cynthia Nelson of Magnolia Springs, Alabama, which I would love to have you come down and visit, it is a beautiful little community, they are concerned that with the SEC agreeing to stipulations that they were not supposed to have agreed to on behalf of the victims, that it jeopardizes their ability going forward to recover funds. I know the SEC has appealed the District Court's ruling, so technically it is still up in the courts.

But if you had an opportunity to visit with my constituents or others from wherever of the 50 States and territories, as Mr. Serrano likes to remind us, if you were sitting down with them, what would you say in terms of the SEC's handling of this to date?

Ms. WHITE. Well, first I would obviously express, as I am sure you and many others have, the deep regret that they have suffered

the loss that they have suffered. I mean, this is obviously a huge Ponzi scheme with pervasive illegal conduct that harmed many, many people.

I think with respect to the SIPC issues and the lawsuit, my understanding of that is, and I have looked into it factually, at least to some degree, is that I think for the first time actually in the SEC's history, and this was really in pursuit of trying to redress the harms that were done to your constituents and other investors, the SEC instituted an action to require the initiation of a SIPC liquidation. That is the lawsuit that the SEC lost in the District Court, as I understand it, on a legal theory that I think was essentially unrelated to the factual stipulations that you are referring to. Certainly, as I understand those, either unrelated to the legal theory or consistent with the legal theory, the SEC's legal theory being that even though your constituents may have invested in let's call it the Stanford bank rather than the broker-dealer, that in effect the broker-dealer that is covered by SIPC constructively had their moneys too, which would mean that they would be covered by the SIPC Act.

So that is something that we obviously disagree with the District Court's decision in that. The SEC really did and has and will continue to pursue that very, very aggressively. But I think from what I know of the litigation, that is how it came to rest where it came to rest, and now it is on appeal and the SEC is obviously pursuing that vigorously.

Mr. BONNER. Shifting gears, thank you. The organizational structure of the SEC has been a longstanding problem, certainly long before you arrived in your current position, with more than 20 different divisions and offices all reporting directly to the chair. In the 2010 report, the Boston Consulting Group identified a need for a significant reorganization as one of four priorities, and it is my understanding that the SEC has submitted to Congress three of four reports on implementation of the BCG recommendations as required, yet to date the only reorganization the SEC has undertaken has involved an administrative support of offices, as I understand it.

So two observations and a question. One of the major issues identified by the Boston Consulting Group report was a lack of a formal structure to resolve disputes between major SEC offices. Can you tell us what actions you will take as the SEC chair to address the silo problem that exists under the current SEC structure? And secondly, as the new chair will you act on the recommendations of the Boston Consulting Group and undertake a comprehensive reorganization of the operating divisions of the SEC?

I will say at the outset, being from Alabama as well as the State of Florida where the chairman is from, the distinguished chairman, the SEC in our part of the world is the Southeastern Conference. So I know the difference between the two when I ask the question.

Ms. WHITE. Actually, I asked for that job but no one would give it to me.

But let me just say that I think the fourth of those, which is the final of those reports, I think was just submitted to Congress from the SEC. My understanding is that there were essentially 20 sets of recommendations for new initiatives, including some of the re-

structuring recommendations that were made by the Boston Consulting Group, and 16 of those 20 have actually resulted in an implementation plan and the other four are continuing to be worked on.

My further understanding is that in terms of some of the restructuring suggestions actually before the Boston Consulting Group was retained, the Enforcement and Examination Divisions of the SEC underwent significant restructuring, I think to very good ends. I have been there one day less than a month, I guess, but it will be something I will be looking at across divisions. And also responsive to the recommendations, each of the other major divisions has a managing executive now too, which I think has been a real management enhancement. That grew out of the Boston Consulting Group review as well.

The SEC has moved on to what I call the support operations of the organization. One recommendation, for example, from the Boston Consulting Group was to merge the executive director of the SEC with the COO's office. That has been done, I think to a very good end and very good efficiencies. I will be looking across the agency obviously for further enhancements and improvements, but I think the SEC has made significant progress based on those recommendations and their own initiatives.

In terms of siloed information, that is obviously something that you need to deal with in any organization because you will not function effectively with the silos. I think my management style is to break down silos anyway. I think my predecessors achieved a lot of progress in that arena as well, and certainly I bring everyone together to do that and hopefully will walk the walk and talk the talk as well. So I look forward to doing it.

Mr. BONNER. Thank you, Mr. Chairman.

Mr. CRENSHAW. Thank you. Mr. Quigley.

Mr. QUIGLEY. Thank you, Mr. Chairman.

Madam Chairman. Last year as you know we passed a couple measures that required companies that file with the SEC to disclose information about their dealings with Iran. The first question is do you have the resources to make sure that there is compliance with that requirement, those requirements?

Ms. WHITE. Again, one of the divisions where we are seeking I think 25 additional positions is the Division of Corporation Finance, which actually is the division charged with the review of public companies' filings. The Iran requirement became effective, as I recall it, in February of this year in terms of filings made, and I think we have received now, if I have my number right, 242 such filings to date, and I think that is really up-to-date. Somebody gave me the number I think yesterday or today. The Division of Corporation Finance selectively reviews filings, including those with Iran disclosure.

We also require that those making those disclosures give notice on EDGAR that they have made such a disclosure, which helps one not to lose it in the bulk of the disclosures that are made. We then give immediate notice to Congress, the President, Treasury and the State Department so that they can pursue that. So it is an area in which we certainly are carrying out our functions. It is obviously

a relatively new set of disclosures that we are reviewing for the last few months, but it is very important that we do so.

Mr. QUIGLEY. Let me know if I am mistaken here, but I have had people address concerns that the Chinese energy firms, two of them, have failed to meet the specific requirement about these level of disclosures that they have with the government of Iran. Is that your understanding and where are we at with that issue?

Ms. WHITE. I would be happy to get back to you on the specific instances that you mentioned. Clearly as a process matter what should happen if there is deficient disclosure is the usual comment back and forth between Corporation Finance and those companies should be occurring. But I am happy to get back to you on the specifics of that.

[The information follows:]



**FINANCIAL SERVICES AND GENERAL GOVERNMENT SUBCOMMITTEE  
HEARING ON THE SECURITIES AND EXCHANGE COMMISSION**

**QUESTION FOR THE RECORD**

**CONGRESSMAN MIKE QUIGLEY**

**At the May 7, 2013 hearing of the Financial Services and General Government Subcommittee, Congressman Quigley asked the following:**

**And let me know if I'm mistaken here, but I've had people address concerns that Chinese energy firms, two of them, have failed to meet the specific requirements about these level of disclosures that they have with the government of Iran. Is that your understanding? And where are we at with that issue?**

**RESPONSE:** With respect to the particular companies you identified, I understand that SEC staff reached out to yours in an attempt to gain more information. While we are unable to speak publicly about specific companies or their compliance with specific disclosure requirements, I can talk generally about how the SEC would approach a situation where it appears that material disclosures are not provided in the course of a review of a company's disclosure filings.

It is worth noting up front that SEC staff does not review every filing of each reporting company every year. Section 408 of the Sarbanes-Oxley Act requires the review, at least once every three years, of the disclosures, including financial statements, of each company required to file reports with the Commission, which currently totals approximately 9,100 companies. In addition to these reviews, staff in the Division of Corporation Finance selectively reviews additional periodic reports and documents that companies file when they engage in public offerings, business combination transactions and proxy solicitations. On the whole, Division staff annually review filings of a substantial number of the companies that are required to file reports with the Commission. In fiscal 2012, the Division reviewed the filings of more than half of the reporting companies.

During the course of these reviews, Division staff members often monitor press, analyst activity, market trends and listen to earnings calls so that they are able to identify issues that may represent material trends or material company-specific issues. In addition, with the assistance of the Division's Office of Global Security Risk, Division staff members continue to monitor filings for disclosure of global security risk issues.

During this process, staff may send a company a comment letter with suggestions on how it can improve its disclosure or enhance its compliance with the applicable disclosure requirements or ask questions with respect to compliance

with disclosure requirements. When issuing comments, the Division may request that a company provide supplemental information so the staff can better understand the company's disclosure, provide revised or expanded disclosure in a future filing with the Commission or amend a document on file with the Commission to revise or expand disclosure. To enhance the transparency of the review process, no earlier than 20 business days after the review is complete, the Division makes the comment letters and company responses to them available to the public.

Mr. QUIGLEY. I would appreciate it. And last, the SEC recently filed charges against my home State, the State of Illinois. The quote was that Illinois misled municipal bond investors about the State's approach to funding its pension obligations. Now, for those of us in Illinois, pension troubles are no surprise. There is nothing new. It continues to be a major issue.

But can you elaborate to any extent on how Illinois was able to mislead investors? Obviously this is an ongoing situation, but would setting disclosure standards for municipal issuers help avoid this kind of issue in a more generic sense?

Ms. WHITE. The answer is it is a priority of the SEC to deal with the disclosures in municipal financing.

Mr. QUIGLEY. Illinois is not alone.

Ms. WHITE. Illinois is not alone. I believe this is the case, this is our third major action of this kind and it remains a priority, so they are definitely not alone. Obviously we are talking about enforcement actions. The SEC has also made recommendations in a report to Congress about, among other things, enhanced disclosures. We don't have powers over those disclosures as we sit here now except through the broker-dealers who actually do the financings themselves. But it clearly remains an issue.

Mr. QUIGLEY. We didn't set standards I would assume you would think, right? I know you don't have the powers, but someone needs to set these.

Ms. WHITE. No, I think you certainly want that disclosure to be more robust than it has been and we certainly see those issues, and not just in your home State but in others with respect to underfunded pension plans and other issues frankly as well. It is a market that needs real attention.

Mr. QUIGLEY. I appreciate that and I appreciate your getting back to us as you suggested and following up on the issues dealing with the disclosures of ties to Iran.

Ms. WHITE. Happy to do that.

Mr. QUIGLEY. Thanks for your service.

Mr. CRENSHAW. Thank you. Mr. Womack.

Mr. WOMACK. Thank you, Mr. Chairman, and congratulations, Madam Chairwoman, and I wish you the very best in this position.

As you know, the JOBS Act was signed by the President in April of 2012 and it provided language in there that provided a year for the implementation of regulations, and it has been a little more than a year. Can you fill me in on where we are in that process? I know you are new to the job here, but where are we in the process?

Ms. WHITE. Again, what I can say is, and I said it at my confirmation hearing and I think I mentioned a little bit earlier, but my top priority, I mean I guess I identified three immediate top priorities, is to get the Congressionally mandated rulemaking done, and that is Dodd-Frank but it is also JOBS Act. I am spending a great deal of my personal time in driving those rulemakings. I can't give you a specific timetable. They are under active discussion with the staff and the Commissioners. But I am absolutely committed to getting them done as promptly as possible.

Mr. WOMACK. Even though you can't give a specific timetable, can you give us a season maybe?

Ms. WHITE. That might not tell you anything I guess if I gave you a season. All I can say is that we are actively engaged in that process.

Mr. WOMACK. This year?

Ms. WHITE. As we speak.

Mr. WOMACK. Will it be this year?

Ms. WHITE. I certainly hope so.

Mr. WOMACK. Okay. Among other things, the JOBS Act had some shareholder registration and deregulation, or deregistration thresholds for bank and holding companies. Unfortunately, it did not explicitly extend those new thresholds to the savings and loan holding companies, even though Congress did not intend to treat them differently. And by the way, there has been legislation filed, in fact it was in Financial Services today, it got a voice vote, but my understanding is that the SEC has the authority to extend the new thresholds to the savings and loan holding companies.

Why at this point has the Commission chosen not to do that? Is that something that you are tracking?

Ms. WHITE. I am tracking that, and my understanding is that it is still under discussion and consideration whether we can do that by rulemaking. But that is something I am focused on and will remain focused on. I am very aware of that issue and indeed have been in discussions as early as this week on it.

Mr. WOMACK. Well, just thinking out loud, if there was a positive opinion registered about do you have the authority to extend that threshold, would it be your intent to extend it?

Ms. WHITE. Again, my understanding is, and, again, I don't want to get ahead of the internal discussions or my legal advisers at the SEC, but I think—

Mr. WOMACK. Hypothetically.

Ms. WHITE. But I think the sense is that this was an oversight that should be corrected.

Mr. WOMACK. And we agree with that. That is all the question I have, Mr. Chairman. Thank you.

Mr. CRENSHAW. Thank you. Ms. Kaptur.

Ms. KAPTUR. Thank you, Mr. Chairman, and welcome, Ms. White. I am really glad to have you here today and wish you well in your new duties.

I have two questions. The first is kind of to provide some perspective. In order to prevent major financial calamities in the future, retrospectively going back to the 1980s and 1990s, can you unwind the market shifts in housing investment instruments that caused the financial crisis and why the SEC failed to capture their risky nature early on? Kind of looking back. And what do you know now that you didn't know then? What could you be looking for? What footprints were out there that for some reason was not caused by an agency that spends \$1.5 billion a year?

Ms. WHITE. Well, I think it goes beyond the SEC. I think we are trying to appreciate more what folks missed and didn't understand, and we are trying to regulate better to prevent that from repeating itself in the future.

I think the SEC is predominantly a disclosure agency, and so one of the things you want to be sure of is that investments tied to the real estate market, securitizations and the like, have the full range

of disclosures. That is something that indeed we are mandated under Dodd-Frank to attend to and we have attended to under Dodd-Frank so the disclosures are out there for people to see. I think the theory of our regulation at the SEC is that good full disclosure to investors can prevent a lot of harm that occurs otherwise.

Ms. KAPTUR. But could you for those of us who don't spend our time in the financial markets extending risk beyond what would be prudent, what really happened?

Ms. WHITE. I am not sure I or anyone can quite answer that. In terms of the housing market?

Ms. KAPTUR. Yes. I mean you had a loan, it turned into a bond, and then the bond into a security that was sold internationally in tranches. How did that, from a historical standpoint, who started that and how did it flower inside our financial system without apparently all these regulatory agencies understanding the full nature of how very risky that was? How was that possible?

Ms. WHITE. Well, I think, again, commissions, committees and others, experts have spent a lot of time gathering a lot of information specifically with that retrospective kind of look and come out with actually differing conclusions to some degree. So I wouldn't profess to have that degree of knowledge on this to respond to your question.

But I would say that I think the downturn in the housing market has occurred. I think it did occur to the surprise of many. Why did that happen? If there had been better disclosure, better attention paid to that, would we have caught it earlier? Certainly those are among the conclusions that others have reached. Why were there securitizations? Again I think from the SEC's perspective, we are a capital markets regulator. Investors make their choices in different investment products. Our job, and it is a big job, is to make sure that the disclosure that they are given with respect to those investments are full and fair so that they can make informed decisions.

Ms. KAPTUR. Are you saying that the collateralized debt obligations, for example, had no disclosure? The problem was that it wasn't disclosed at some point?

Ms. WHITE. I think there have been many examples including I think in the enforcement arena where the disclosures were not adequate, no question about it. The SEC has brought quite a number of quite important cases with respect to structured products, the deficiencies, and the disclosure that accompanied them.

Ms. KAPTUR. Well, don't you think it is awfully important to totally understand where the system failed in order to fix it?

Ms. WHITE. I think there is no question about that.

Ms. KAPTUR. How could the government of the United States have missed this?

Ms. WHITE. Well, you know, again, that is a broad question. I know it is intended to be a broad question. It is something that I think—it is a multi-factored, very complicated picture. I don't think it is a simple one. And as I say, many committees and commissions, have spent a lot of time, a lot of investigative efforts doing that retrospective look. Plainly what we are doing going forward is designed as a government, as a U.S. government, to prevent that

kind of crisis from occurring again, and to prevent the kind of systemic risk that could be introduced into the system. That is something that everybody, not just the SEC, but all the regulators are very much focused on.

Ms. KAPTUR. Are there not certain types of derivatives, for example, where disclosure will not be required? They were exempted under Dodd-Frank?

Ms. WHITE. Well, I think what Dodd-Frank has essentially done is, among other things, mandated rulemaking to regulate the over-the-counter derivatives market. It was not regulated before essentially.

Ms. KAPTUR. But there are some exemptions, are there not?

Ms. WHITE. There are.

Ms. KAPTUR. Yes, and what might those be?

Ms. WHITE. Well, there are different exemptions depending upon what arenas we are talking about. There are various exemptions, for example, from the Volcker Rule in terms of proprietary trading. I don't want to—there are certain exemptions with respect to hedging activities for customers, which is certainly needed to occur or the market making exemption.

There are exemptions—what you don't want to do when you regulate and respond to a crisis is to over regulate beyond what you are intending to do so that you actually cause harm you are not intending to cause. So it is a massive effort. It is a massive effort that has been assigned to the regulators to sort out with statutory prescriptions, but as smartly as we can, exemptions included.

Ms. KAPTUR. Mr. Chairman, I know my time is up, but it seems to me incumbent upon all the regulatory agencies and this White House to understand in sheer utter detail where the train started going off the track in the late eighties and early nineties. By the mid-nineties we were already positioned for a major catastrophe forward and the instruments that were created were not detected.

It seems to me that there needs to be a postmortem here by important regulators like yourself. And to the extent you could provide to the record, maybe talking with some of your colleagues now responsible for regulation, let us know looking back retrospectively where those instruments were created, what year, by which institutions, that ultimately led to very high risk behavior and instruments that the regulators missed and when that happened.

It just wasn't spontaneous combustion. It was actual actions by individual institutions and very high risk behavior that was undetected inside our system and has resulted in the largest transfer of wealth in American history from Main Street to Wall Street and the loss of a majority of equity, for example, in the African American community of this country.

It is a shift of wealth that is extraordinary, and I think it would be important for the SEC staff and for the Commission itself to understand where the train started going off the track back in the early nineties, late eighties—early nineties.

I thank you very much for your appearance today. Thank you, Mr. Chairman.

[The information follows:]

For information, please refer to the insert titled "Questions for the Record From Congresswoman Kaptur".

Mr. CRENSHAW. Thank you. Mr. Yoder.

Mr. YODER. Thank you, Mr. Chairman. Chairman, thank you for being here today and congratulations on your new appointment. We look forward to working with you.

The SEC recently proposed a 650-page rule on the cross border application of the Dodd-Frank law to security based swaps. First of all I want to commend you, Chairman White, for issuing a proposed rule in accordance with the Administrative Procedures Act which governs the way in which administrative and independent agencies may propose and establish regulations and mandates cost-benefit analysis and notice and comment from regulated industries.

As you may know, the CFTC has taken a different route. It also has regulatory responsibilities for cross border swaps. However, instead of engaging in a formal rulemaking process under the Administrative Procedures Act, CFTC Chairman Gensler has chosen to issue interpretive guidance without the approval of commissioners. That has resulted in some challenges for those folks that deal in those industries. And we have had major G-20 regulators from around the world commenting that the guidance from the CFTC is flawed and will cause major economic challenges in relations in terms of regulation between these countries.

I guess first of all why did the SEC choose a rulemaking procedure as opposed to a guidance as the CFTC has chosen and what benefits does that offer?

Ms. WHITE. I think I would say in response to that that the ordinary course for the SEC is to engage in notice and comment rulemaking. Obviously we can give certain guidance from time to time and proceed differently.

These are extraordinarily complex regulations. The market is uniquely global. The complexities really are quite extraordinary. We were pleased to put out, actually unanimously last week, a very robust rule we think that is out again for public comment. We have gotten pre-proposal comments as well. We have been engaged in very active dialogue with the CFTC. We have studied the comments they got on their interpretive guidance. We have been in discussions with many other commenters and we will be now that the rule is actually proposed, including our foreign regulators.

We really need to get this right. Obviously we are trying to prevent the risk to the U.S. from this marketplace, but to do it wisely and in full consultation and as smartly as we possibly can. It is not easy to do. We obviously will listen to all views now that the rule is out, but we were quite pleased to put it out last week.

Mr. YODER. Well, I appreciate that, and I certainly appreciate the collaborative approach of building consensus that has occurred at the SEC, and I am very concerned about the CFTC's language, as are certainly foreign regulators. I guess what can the SEC do to work with the CFTC to ensure that there is some consistency between these things? Certainly there are unique areas of regulation and that is why we have both the CFTC and the SEC involved in their own separate processes. But as you can imagine the complexities that exist already in this area of financial regulation and to have two agencies who may have separate regulations, some of which at the CFTC may make it impossible for foreign regulators to have a role because of the constraints put in place, I guess how

can you and the SEC play a role in ensuring that both procedures are done in a way in which, since you are regulating many of the same folks, can be consistent in their application?

Ms. WHITE. Our mandate is to coordinate and consult with the CFTC. I think everybody recognizes that it would be optimal if there was consistency. The markets are somewhat different. There could be some differences. I would say with respect to the interpretive guidance that the CFTC has put out as well as some of what they have said in some of their no action exemption measures, there are a lot of consistencies between the SEC and the CFTC. But it is very important to continue this dialogue because it is a uniquely global market with regulators around the world who are in this space and very focused on it.

So we are going to continue in dialogue with the CFTC and with our foreign counterparts to try to do as best we can to be consistent and put out the best possible rules on this, carry out the statutory objective, but also to take cognizance of how global and complex this market is.

Mr. YODER. Thank you for that. I have a question on a different topic, if I might, Mr. Chairman, if I have a couple minutes.

The Fourth Amendment to the Constitution speaks to the right of people to be secure in their persons, houses, papers and effects against unreasonable searches and seizures. There is legislation being introduced in the House and the Senate related to the privacy rights of individuals related to their email. There have been some agencies that have opined that individuals do not have an expectation of privacy when it comes to their email correspondence. I happen to strongly disagree and believe that Americans expect that their email is not being read by the Federal Government. We have instances where this is happening without the knowledge and without any sort of approval process from the Judiciary. It is essentially self-executing powers by Federal agencies.

There is a bill in the Senate, there are bills being introduced in the House related to this. And I guess first of all, do you think this is an appropriate power that these agencies hold, yours included, that allows these departments to read individuals' emails without any sort of oversight by the Judiciary? No check on that power. And if you think about any other situation in your home or your personal papers, the Fourth Amendment protects those rights, that without a warrant or without proper oversight that we have a reason to expect our own privacy.

Do you think that is appropriate and would you support legislation to restrict those powers in a way that still keeps the investigatory tools of the SEC but respects the privacy rights of email for the individual?

Ms. WHITE. Well, there is no question that privacy interests are extremely important. I mean, I think we have actually weighed in with a letter. I believe we are talking about the same piece of legislation. The SEC, among other agencies, will in its enforcement function in particular subpoena emails from individuals and also subpoena them historically from Internet service providers.

I think the current legislation, we have a worry from our enforcement perspective, sweeps too broadly there with regard to Internet



service providers, because it can result in our not being able to issue those subpoenas.

You could have a system that requires a search warrant for those. I think that some have advocated that. We obviously don't have the search warrant powers in the SEC. The Justice Department has that, where if you got a warrant you would have to go before a judge before you could do that. But I think we have to be very careful that we aren't really gutting the enforcement powers. I think we have to be very sensitive about the privacy interests, but I do worry about aspects of that legislation.

Mr. YODER. Do you think the current powers the SEC holds are appropriate given the Fourth Amendment right to protection and right of privacy without unnecessary searches by the Federal Government?

Ms. WHITE. I do.

Mr. YODER. Okay. Well, we are going to have a debate about that in Congress, and many of us disagree, and we think that Americans do expect that they have a right to privacy in their email, and the idea that the IRS or the SEC or any Federal agency would be reading their emails without due cause or without any sort of oversight from the Judiciary that we use for every other portion of our lives, whether it be our person, our effects, our papers, our housing, that somehow email would not have the same expectation of privacy is a real issue for a lot of Americans. I think it is something that Congress is going to debate.

We would love to have a partnership in ensuring that we have a way to continue to have proper investigatory powers, but the status quo is completely unacceptable to many Americans and I think it is going to be something that Congress is going to have to address.

Ms. WHITE. I appreciate those comments completely and I will make sure we are not ships passing in the night. What I am really referring to is the Enforcement Division subpoenaing of emails, not reading them realtime. So I take your point.

Mr. YODER. Thank you, Mr. Chairman.

Mr. CRENSHAW. Thank you. I think we will have time if people have another question, but I would like to ask you one final question and that is about money market funds. The SEC regulates them. I think most people know those to be among the safest investments. You put a dollar in and you are supposed to be able to get a dollar back, so it is a great short-term investment.

As you know, in 2008 during the meltdown it wasn't the case. They called it breaking the buck. When you put a dollar in and there was a run on those money market funds, then there was a time you only got back 97 cents. As I understand there is nearly \$3 trillion in money market funds. I know it is something you all are thinking about proposing some rules for, and any time when people start talking about rules there is concern that somehow they could have a negative impact, such as increase the borrowing costs, or change the nature of the instrument.

Can you just comment very briefly on what your view of that is? Is that something you take into consideration as you try to safeguard these financial instruments? And also, are there any other short-term vehicles that you know of that would be alternatives?

Because these are used, as you know, by individuals, by businesses, by States, and municipalities. Please talk a little bit about your view of reform of the money market funds.

Ms. WHITE. First, I agree that they are very important products, both to investors and those companies who engage in short-term borrowing. And you cite the incident in 2008 obviously the cause of great concern and runs on the funds so-to-speak. The concern is the systemic risk and also that retail investors may be late to the party in redeeming, and so you need to sort that out and deal with those phenomena. And the SEC in 2010 actually did engage in rulemaking which I think did increase the resiliency of the money market funds. We are engaged in further discussions about further reform, and I am expecting the staff to make recommendations to the Commission in the near future.

But as we do that, talking about economic analysis, we have gotten from our economists at the end of last year an excellent study that was in response to three of our commissioners' questions that was directed to impact kinds of questions, what may have caused the runs on the funds, et cetera, and what the effect of various reforms might be. So that is a very important study in our analysis. And also as we engage in this discussion and further reform, we want to do what we can not to harm the product as well.

Mr. CRENSHAW. Thank you. I think that is important. As you know, when the government came in to insure those, nobody lost any money and we are through that difficult time. But I think that is an important short-term investment vehicle that so many people use and it is important to our economy. Thank you for that.

Mr. Serrano.

Mr. SERRANO. Thank you, Mr. Chairman.

Chairman White, I think the SEC has been more vigorous than ever in pursuing wrongdoing. However, I am concerned about the various reports regarding the SEC's settlement policies with those accused of unlawful activities. In some cases the SEC has obtained settlements with individuals in which they do not have to deny or admit guilt even though these same individuals have pled guilty to criminal charges elsewhere.

Do you think the SEC is doing enough to obtain admissions of guilt in settlement agreements and do you think the SEC can obtain enough deterrence value from a verdict in which an entity doesn't admit any wrongdoing? And part of the question will be if you had all of the funding that you needed, could you then devote to trying to get convictions, if you will, or admissions of guilt, or is this just a policy that says that this may be one of the few places where people don't ever have to admit they did anything wrong?

Ms. WHITE. I have several responses to that. I guess first, the no admit-no deny settlement protocol has been used not only by the SEC but a number of agencies. This is on the civil side. Obviously the SEC doesn't have criminal powers for many, many years, and I think to very good end in many cases, where you essentially get nearly all and perhaps all, sometimes more of the relief than you would get after you litigated and you have no litigation risk whatsoever. You get that money to the investors very quickly.

The SEC has actually changed its policy in cases where there is a parallel criminal matter, where the Department of Justice, for ex-

ample, will get admissions as part of their resolutions with institutions. The SEC also at least generally will get those admissions as well. So having said that, among the many things that I am reviewing as the new chair is that policy and protocol.

I understand the desire for accountability not only by institutions but individuals, but I will also say that the SEC's settlements, whether they are administrative or they are judicial, lay out a very detailed statement of facts so there is no real question about what the conduct was.

But I take your point, and among the things I am reviewing with the Enforcement Division is that policy.

Mr. SERRANO. Well, that is good to hear, because, you know, one of the comments, and again I mentioned to you some of the comments that we make amongst ourselves when we are on the House floor before a vote or doing a vote or whatever, in the elevator, is that 2008 was such a dramatic thing that happened in our country, such a fiscal tragedy, if you will, fiscal crime in many cases, and yet the feeling from most Americans are that no one paid a price for that, other than the investors and the economy and the American people, that no one went to jail for that.

So how confident are you that we as a body and you as an agency can convince the American people that folks are not going to get away with something, at least get away with it again?

Ms. WHITE. Well, first, I think it is absolutely essential for not only the SEC's enforcement function but any prosecutor, any enforcement function, to have credibility with the American people, that when there is wrongdoing there will be detection, there will be aggressive pursuit and investigation, and there will be punishment and accountability.

I would say that I think the SEC doesn't, of course, have the criminal power, so it doesn't have the ability to put anybody in jail. But I would say that I believe that the SEC's record in financial crisis cases is really quite impressive. Essentially they brought cases I think against 157 individuals or entities. They got either disgorgement or other penalties, \$2.6 billion, most of which goes to investors. Sixty-six I think of the individuals that they charged were CEOs, CFOs or other senior executives. I think 70 percent, if I am recalling it correctly, of the financial crisis cases against individuals were brought as litigated cases. So that is not a situation where that began as a no admit-no deny situation.

And I don't want to imply that I don't think, even after our review of various policies—I think there is a significant role for no admit-no deny settlements in every civil agency, because it saves resources, you do not incur the litigation risk, and you get lots of money to investigators a lot quicker. But nevertheless I will be reviewing the scope of that.

Mr. SERRANO. Well, we appreciate that.

Mr. Chairman, I will have a couple more questions for the record. But let me just thank you for your service in general to our country and specifically now in this position. And your challenge, which I am sure you know, is partly due to your success in your other positions that you have held, so many people have sighed a sigh of relief knowing that someone now is going to be really scrutinizing the situation. And that is the challenge we have as a Con-

gress and the challenge you have personally. But we know you are up to the job and we congratulate you again.

Ms. WHITE. Thank you very much.

Mr. CRENSHAW. Ms. Kaptur, do you have another question?

Ms. KAPTUR. Yes. I wanted to continue and ask, for most of my adult life people got mortgages as loans and generally the local bank held it or sold it off into the secondary market. But at what point did that loan, to your knowledge, did it become a mortgage backed security? The name of your regulatory body is the Securities and Exchange Commission, so I take it that your agency would be particularly knowledgeable about when the instrument turned from a loan to a mortgage backed security. Am I correct in my understanding?

Ms. WHITE. I am sure the agency is very knowledgeable about that. I believe that the securitizations such as you are referring to I think began, that product I think began to be used in the 1980s, I believe.

Ms. KAPTUR. Yes. I would be very interested for the record, unless you unwind why your ship crashed you are likely to do it again. So I am very interested in how that occurred and how it eluded the regulators within the SEC in terms of its riskiness. I am wondering what happened. And many institutions then having those loans put into some other place and retaining no ownership at all in that loan, what happened and which institutions.

Would your commission have the ability to identify through its records which financial institutions first brought those deals forward?

Ms. WHITE. I don't know which institutions. I think there are public reports that talk about this. I don't think the fact that securitizations were occurring was unknown to the marketplace. Once it developed in the 1980s, I mean, the market was an active one and I think not an unknown market. I think again what I had said earlier is I think reflected certainly in our enforcement cases is what was the disclosure about those securitization products.

Ms. KAPTUR. Yes. And there are institutions, I understand one of them is in Illinois, that actually pivoted off of auto securitization into home mortgage securitization, and back about, oh, the early 1990s I think had the largest fine in American history placed on it by the Office of Comptroller of the Currency. I am remembering back about \$450 million, it was the largest ever placed on an institution at that point in American history. So something went wrong there.

What is of interest to me is knowing that, how was it that that process was allowed to move forward and not carefully regulated by the SEC, since they were securities? What was missing in the law or your regulatory authority? How did that instrument elude regulation? Are you able to tell me that by going back through your legal staff?

Ms. WHITE. We can certainly provide further information for the record in response. But, again, I think we are talking about, as we are speaking now anyway, about disclosures about these securities.

Ms. KAPTUR. Correct.

Ms. WHITE. But we can certainly try to elaborate on that for you.

Ms. KAPTUR. And I am trying to understand what was it about that moment that created this force inside the financial system that went unregulated? I mean, it is truly extraordinary. So I don't remember anything like it in my adult lifetime. So I am really interested in how you as a commission viewed that moment in history, the people who were in place, because I think we can learn something from it. And how it avoided regulation, how it went undetected by the SEC for all those years.

You weren't the only place, but you do have the title Securities and Exchange Commission. So I am wondering was it the definition in the law that was flawed, was it some mysterious financial instrument that eluded regulation? What happened back then? Could you go back and ask your staff to take a look at that and tell us what occurred back then that allowed for this securitization and the various instruments that were used? I think one was called an RBS, it was a security. I don't know if collateralized debt obligations came under your purview or whether that was over at the CFTC. I am not sure.

But something happened with these very high risk instruments that went undetected. What was the pattern of that instrument inside your commission? Was it even seen? You know, I am thinking back, you know, what happened there? Was it our fault as a Congress that something was exempted from the law?

I am wondering if you could provide enlightenment by going back to that period in time and see why those types of securities involved in the mortgage crisis were not regulated by the SEC. I am looking backward now, not forward. I am trying to understand what happened. Do you have the ability to do that?

Ms. WHITE. I think what I should probably do is let me see if I can give you a further response after I go back and speak with the staff on this. Again, let me do that.

[The information follows:]

For information, please refer to the insert titled "Questions for the Record from Congresswoman Kaptur".

Ms. KAPTUR. Thank you very much. Then my second question and my last question for the record, looking forward, if you look at the cases that have come from the SEC now that have yielded some compensation back to individuals who have been harmed or regions that have been harmed, could you suggest which of those might have been the most effective in moving dollars back to individuals and communities that have been harmed? What were the causes of action that were the most, to date, the most effective in getting justice to harmed individuals and communities?

Ms. WHITE. I think the financial crisis cases that I just mentioned in terms of the numbers of dollars, the high volume of dollars, I mentioned \$2.6 billion that the SEC has achieved through those financial crisis cases either by way of disgorgement or penalties, most of which goes back to investors, I think those cases have been very successful.

I think by definition you want every harmed investor to get as much compensation as possible. Obviously we have been talking about scarce resources, but I think those cases actually delivered a lot of money back to harmed investors very successfully.

Ms. KAPTUR. Is your commission aware or could you provide for the record any communities across this country where, for example, a city, county government, a school district, had pension funds or investments that were impaired by certain financial companies that gave them faulty advice or fraudulent advice and therefore those funds lost money, impacting those communities. To your knowledge have there been any such investigations by your commission or any communities that have been found that experienced that type of loss and has that been litigated?

Ms. WHITE. Certainly people across this country in all communities can suffer losses at the hands of a securities fraud, and certainly the SEC has brought cases that have pursued those and pursued those in many cases to achieving a fund for investors in various communities. But I can try to respond further for the record.  
[The information follows:]

**FINANCIAL SERVICES AND GENERAL GOVERNMENT SUBCOMMITTEE  
HEARING ON THE SECURITIES AND EXCHANGE COMMISSION  
MAY 7, 2013**

**Questions for the Record from Congresswoman Marcy Kaptur**

At the May 7, 2013 hearing of the Financial Services and General Government Subcommittee, Congresswoman Marcy Kaptur asked a number of questions relating to the residential mortgage-backed securities market, including:

- When these instruments were created and by which institutions;
- What allowed for the securitization markets and high-risk instruments to develop;
- Was the Commission aware of these instruments; and
- How was the Commission regulating these instruments or were they exempt from regulation.

In connection with these specific questions, Congresswoman Kaptur also asked for an overview of the development of the residential mortgage-backed securities market, and how, from an historical standpoint, did regulators fail to understand the full nature of the risks relating to these instruments. The following summary of the development of residential mortgage-backed securities market responds to these questions.

**Overview of Asset-Backed Securities**

Generally speaking, asset-backed securities are securities that are backed by a discrete pool of self-liquidating financial assets, such as loans. Asset-backed securitization is a financing technique in which financial assets, in many cases themselves less liquid, are pooled and used to fund securities that may be offered and sold in the capital markets.<sup>1</sup> This allows the lender to receive money for the loans soon after they are originated, providing the lender with funding that it can use to make more loans or extend more credit. In a basic securitization structure, an entity, often a financial institution and commonly known as a “sponsor,” originates or otherwise acquires a pool of financial assets, such as mortgage loans or credit card receivables. It then sells these financial assets to a specially created investment vehicle that issues securities “backed” or supported by those financial assets. These securities are “asset-backed securities” or “ABS,” and they are typically sold to institutional investors. Payment to investors on the ABS is made primarily from the cash flows generated by the assets in the underlying pool.<sup>2</sup>

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<sup>1</sup> “Securitization” is a commonly used term to describe this financing technique, although other terms, such as “asset-backed financing,” also are used.

<sup>2</sup> See Asset-Backed Securities, Release No. 33-8518 (Dec. 22, 2004) [70 FR 1506], at 1508.

Residential mortgage-backed securities (“RMBS”) are ABS backed by some type of residential loans, including traditional mortgage loans and equity lines, or backed by other RMBS. In the basic RMBS structure, a group of mortgage loans is sold to a trust or other investment vehicle, which owns the mortgage loans and sells securities that are backed by the loans. A servicer collects payments from the borrowers on behalf of the trust, and the trust makes payments on the securities to the investors that hold the RMBS.<sup>3</sup>

At its inception, securitization primarily served as a vehicle for mortgage financing. Since then, ABS have played a significant role in both the U.S. and global economy. Securitization can provide liquidity to nearly all major sectors of the economy, including the residential and commercial real estate industry, the automobile industry, the consumer credit industry, the leasing industry, and the commercial lending and credit markets.<sup>4</sup>

### History of the Residential Mortgage-Backed Securities Market

For decades, the Federal government has worked to facilitate a liquid secondary mortgage market so that lenders may sell the mortgage loans they originate in order to free up capital for other loans.<sup>5</sup> The beginning of the modern RMBS market can be traced to 1970 when the Government National Mortgage Association (“Ginnie Mae”), a wholly owned Federal government corporation, first guaranteed securities backed by a pool of mortgage loans. The creation of the Federal Home Loan Mortgage Corporation (“Freddie Mac”) in 1970 helped to expand the market.<sup>6</sup> Freddie Mac issued its first RMBS in 1971, and the Federal National Mortgage Association (“Fannie Mae”) issued its first RMBS in 1981.<sup>7</sup> For a number of years, RMBS were almost exclusively a

<sup>3</sup> See “Staff Report: Enhancing Disclosure in the Mortgage-Backed Securities Markets” (Jan. 2003) available at <http://www.sec.gov/news/studies/mortgagebacked.htm#exec> (hereinafter, the “2003 MBS Disclosure Report”).

<sup>4</sup> See generally, Release No. 33-8518, *supra* note 2, and *Asset-Backed Securities*, Release No. 33-9117 (Apr. 7, 2010) [75 FR 23328], at 10.

<sup>5</sup> For example, the Federal Home Loan Bank Act of 1932 created a Federal Home Loan Bank system that is designed to attract to the secondary mortgage market, investors who might not otherwise invest in mortgages, making the secondary mortgage market more liquid and expanding the pool of funds available for housing. See Federal Home Loan Bank Act of 1932, Pub. L. No. 72-304, 47 Stat. 725 (Jul. 22, 1932). See also “Government Sponsored Enterprises” available at <http://www.fhfa.gov/Default.aspx?Page=33>.

<sup>6</sup> See Kenneth G. Lore & Cameron L. Cowan, *Mortgage-Backed Securities: Developments and Trends in the Secondary Market* 2-39 (2001), at 1-10.

<sup>7</sup> See Linda Lowell, *Mortgage Pass-Through Securities*, *The Handbook of Mortgage-Backed Securities* 25, 29 (Frank Fabozzi ed., 5th ed. 2001); Freddie Mac, *Key Corporate Statistics* (visited Dec. 12, 2002) available at [http://www.freddiemac.com/corporate/news/corp\\_stats.html](http://www.freddiemac.com/corporate/news/corp_stats.html); Federal National Mortgage Association, SEC No-Action Letter (Nov. 7, 1977). See also Leland Brendsel, *Securitization’s Role in Housing Finance: The Special Contributions of the Government Sponsored Enterprises*, *A Primer on Securitization* 17, 17-29 (Leon T. Kendall et al. eds., 1997).



product of government-sponsored entities (“GSEs”), such as Freddie Mac and Fannie Mae, and Ginnie Mae.<sup>8</sup> As discussed below, over the years Federal laws were promulgated to encourage issuance of RMBS by non-government entities, such as banks and finance companies. RMBS issued by non-GSEs is called “private label” RMBS.<sup>9</sup>

### Secondary Mortgage Market Enhancement Act of 1984

Many of the regulatory constraints that had made it difficult for non-GSE entities to sell RMBS were removed in 1984 with the passage of the Secondary Mortgage Market Enhancement Act of 1984 (“SMMEA”).<sup>10</sup> SMMEA was intended to encourage private sector participation in the secondary mortgage market by, among other things, relaxing certain regulatory burdens that affected the ability of private-label issuers to sell their RMBS.<sup>11</sup> For example, SMMEA allowed state and federally regulated financial institutions to invest in private label RMBS. As discussed below, there were also changes to the Federal securities laws related to SMMEA.

### Effect of Tax Laws on RMBS Markets<sup>12</sup>

Tax law constraints had also affected the types of RMBS that could be sold. Until the passage of the Tax Reform Act of 1986<sup>13</sup> (“1986 Tax Act”), which recognized the Real Estate Mortgage Investment Conduit (“REMIC”) structure with its beneficial tax treatment, most RMBS were sold as “pass-through” securities. Pass-through securities pay an investor principal and interest that mirror the payments received on the mortgage loans underlying the RMBS. These payments on the mortgage loans are passed through the trust to the investors exactly as they are made.

Before 1986, the effect of the limitation on activity of grantor trusts under the tax laws restricted the use of trusts with multiple classes of securities with differing payment

<sup>8</sup> See 2003 MBS Disclosure Report, supra note 3.

<sup>9</sup> There was a small amount of private-label RMBS issuance beginning in the late 1970s. See, for example, Bank of America Nat’l Trust & Savings Association, SEC No-Action Letter (Apr. 19, 1977); Edward L. Pittman, Economic and Regulatory Developments Affecting Mortgage Related Securities, 64 Notre Dame L. Rev. 497, 499 (1989). See, also, Lore & Cowan, supra note 6, at 1-11; Joseph Philip Forte, Capital Markets Mortgage (Apr. 1999) available at <http://www.capitalconsortium.org/docs/capmarkm/htm> (“While some isolated Private Label MBS issuance occurred in the late 1970s, non-GSE securitization of whole loans did not gain momentum until the thrift industry crises in the high interest rate environment of the early 1980s.”).

<sup>10</sup> Pub. L. No. 98-440, 98 Stat. 1689 (Oct. 3, 1984).

<sup>11</sup> The legislation was aimed at encouraging participation in the secondary mortgage market by investment banks, investment entities, mortgage bankers, private mortgage insurance companies, pension funds and other investors, depository institutions and Federal credit unions. See Lore & Cowan, supra note 6, at 1-14. See also Pittman, supra note 9.

<sup>12</sup> See 2003 MBS Disclosure Report, supra note 3, at 8-9.

<sup>13</sup> Pub. L. No. 99-514, 100 Stat. 2085 (Oct. 22, 1986).

characteristics. In this multi-class, or REMIC, structure, the principal and interest payments are not passed through pro rata to all investors as they are paid by the borrowers. Instead the payments on the underlying mortgage loans are divided into varying payment streams to create classes of securities with different expected lengths to maturities, different levels of seniority or subordination or other differing characteristics. Prior to 1986, the tax law treated these multi-class trusts as associations taxable as corporations, and distributions would have been taxable at the trust level and also at the trust investor level. This “double taxation” made multi-class structures generally unfeasible.

The 1986 Tax Act eliminated the double taxation for multi-class vehicles structured as REMICs. With the advent of the REMIC, much more complex structures with multiple classes were developed which divided up the payment streams on the mortgage loans that were collateral for the securities repayment obligations to investors. This change increased the desirability of RMBS investments.

### RMBS and the Federal Securities Laws

RMBS are securities and therefore subject to the Federal securities laws. The first objective of the Securities Act is to provide investors with full and fair disclosure in the offer and sale of securities.<sup>14</sup> The principal vehicle for accomplishing this objective is Section 5 of the Securities Act. Section 5 prohibits the offering of securities to investors through the use of a prospectus, unless the related securities transactions are registered or unless an exemption is available.<sup>15</sup>

The disclosure requirements of the Federal securities laws are intended to facilitate investor access to full and fair disclosure. The Commission’s mandate under the Securities Act and Exchange Act does not include regulating based on the merits of an investment. For example, if a company fully discloses a high degree of risk to investors or financial difficulty, the Commission does not prevent a transaction from proceeding. Rather, the Commission’s role is to require that an issuer of securities disclose these risks so that investors can make informed investment and voting decisions.

### Application of the Registration Requirements to Different Types of RMBS

Not all RMBS are required under the Federal securities laws to register and provide mandated disclosure. There are three principal ways RMBS offerings can comply with the Federal securities laws. First, RMBS issued by the GSEs and Ginnie Mae have been and continue to be exempt from registration under the Securities Act.<sup>16</sup>

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<sup>14</sup> Preamble to the Securities Act of 1933, 73<sup>rd</sup> Cong., 1<sup>st</sup> Sess., 48 Stat. 74 (May 27, 1933).

<sup>15</sup> Securities Act of 1933 §5, 15 U.S.C. §77e (2011).

<sup>16</sup> Ginnie Mae guarantees are exempt securities under Section 3(a)(2) of the Securities Act (15 U.S.C. §77c(a)(2)) and Section 3(a)(12) of the Exchange Act (15 U.S.C. §78c(a)(12)). The

Therefore the GSEs do not need to comply with the Commission's registration and disclosure rules. Second, the public offer and sale of private label RMBS are required to be registered with the Commission. Third, some types of RMBS are typically issued in private placements exempt from registration with the Commission.<sup>17</sup>

### Disclosure and Registration for Private-Label RMBS

RMBS and RMBS issuers differ from corporate securities and operating companies. In most offerings of RMBS, the activities of the issuing entities are limited to passively owning or holding the assets, so there is generally no business or management to describe. Instead, information about the transaction structure and the characteristics and quality of the asset pool and servicing is often what is most important to investors.

Contemporaneous with the enactment of SMMEA, which added the definition of "mortgage related security" to the Exchange Act, the Commission amended Securities Act Rule 415 to permit mortgage related securities to be offered on a delayed basis.<sup>18</sup>

Disclosure in registered ABS offerings largely followed market practices and Commission staff guidance. At the end of 2004, the Commission adopted new rules and amendments under the Securities Act and the Exchange Act addressing the registration, disclosure and reporting requirements for RMBS that are not exempt from registration under the Securities Act.<sup>19</sup> The Commission, in adopting Regulation AB, prescribed specific ABS disclosure requirements for the first time, which are largely principles-based. These requirements included extensive disclosure regarding the assets in the asset pool. While these rules do not restrict the type or quality of assets that may be included

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chartering legislation for Fannie Mae and Freddie Mac contain exemptions with respect to those entities. See 12 U.S.C. §§1723c and 1455g.

<sup>17</sup> A significant portion of securities transactions, including the offer and sale of all collateralized debt obligations ("CDOs") and asset-backed commercial paper ("ABCPs"), is conducted in the exempt private placement market, which includes both offerings eligible for Securities Act Rule 144A resales and other private placements.

<sup>18</sup> See Shelf Registration, Release No. 33-6499 (Nov. 17, 1983) [48 FR 5289]. SMMEA defined a mortgage related security to include a security that has a high investment grade credit rating. As previously noted, SMMEA was enacted by Congress to increase the flow of funds to the housing market by removing regulatory impediments to the creation and sale of private mortgage-backed securities. An early version of the legislation contained a provision that specifically would have required the Commission to create a permanent procedure for shelf registration of mortgage related securities. The provision was removed from the final version of the legislation, however, as a result of the Commission's decision to adopt Securities Act Rule 415, implementing a shelf registration procedure for mortgage related securities. See also H.R. Rep. No. 994, 98th Cong., 2d Sess. 14, reprinted in 1984 U.S. Code Cong. & Admin. News 2827; see also Release No. 336499 (Nov. 17, 1983) [48 FR 52889], at n. 30 (noting that mortgage related securities were the subject of pending legislation). In 1992, the Commission extended shelf registration to non-mortgage investment grade ABS. See Simplification of Registration Procedures for Primary Securities Offerings, Release No. 33-6964 (Oct. 22, 1992) [57 FR 48970].

<sup>19</sup> See Release No. 33-8518, supra note 2.

in the asset pool, the rules are designed to assure that a prospectus contains disclosure regarding the mortgages and structure of the securities that facilitates informed investment decisions. Among other things, the rules adopted in 2004 require extensive statistical pool level information regarding the mortgages, or other assets, disclosure regarding the underwriting standards used to originate those loans and extensive information regarding the performance of loans previously originated and securitized by the same issuer.

### Securitization and the Financial Crisis

Many of the problems giving rise to the financial crisis involved structured finance products, including RMBS.<sup>20</sup> Many of these RMBS were used to collateralize other debt obligations such as CDOs.<sup>21</sup> As the default rate for subprime and other mortgages soared, CDOs and RMBS, including those with high credit ratings, lost their value.<sup>22</sup> As the crisis unfolded, investors increasingly became unwilling to purchase these securities, and today, this sentiment remains, as new issuances of RMBS, except for RMBS guaranteed by the government, remains low.<sup>23</sup> The absence of this financing option has negatively impacted the availability of credit.<sup>24</sup>

The financial crisis highlighted a number of concerns with the operation of some of the securities laws in the securitization market.<sup>25</sup> Certain regulations for ABS rely on

<sup>20</sup> A report by the U.S. Government Accountability Office (“GAO”) notes that 75% of subprime loans were packaged into securities in 2006. See U.S. Government Accountability Office, Financial Regulation: A Framework for Crafting and Assessing Proposals to Modernize the Outdated U.S. Financial Regulatory System (Jan. 2009) at 26.

<sup>21</sup> As noted above, CDOs are typically sold as a private placement to an initial purchaser followed by resales of the securities to “qualified institutional buyers” pursuant to Securities Act Rule 144A. Pools comprising the CDOs may consist of various types of underlying assets including subprime mortgage-backed securities and derivatives, such as credit default swaps referencing subprime mortgage-backed securities, and even tranches of other CDOs.

<sup>22</sup> See, e.g., The President’s Working Group on Financial Markets, Policy Statement on Financial Market Developments, March 2008 (the “PWG March 2008 Report”) at 9 (discussing subprime mortgages and the write-down of AAA-rated and super-senior tranches of CDOs as contributing factors to the financial crisis). CDOs were noted, in particular, to have contributed to the collapse in liquidity during the financial crisis. See, e.g., The Report of the Counterparty Risk Management Policy Group III (“CRMPG III”), Containing Systemic Risk: The Road to Reform, August 6, 2008 (the “2008 CRMPG III Report”), at 53 (noting that lack of comprehension of CDO and related instruments resulted in the display of price depreciation and volatility far in excess of levels previously associated with comparably rated securities, causing both a collapse of confidence in a very broad range of structured product ratings and a collapse in liquidity for such products). Another type of ABS that is privately offered is ABCP, which was increasingly collateralized by CDOs and RMBS from 2004 through 2007. The ABCP market severely contracted during the crisis. See PWG March 2008 Report, at 8.

<sup>23</sup> See Release No. 33-9117, supra note 4, at 11.

<sup>24</sup> Id.

<sup>25</sup> These concerns were outlined in Release No. 33-9117, supra note 4, at 11-12.

the ratings for those securities provided by the ratings agencies, and much has been written about the failures of those ratings accurately to measure and describe the risks associated with certain of those products that were realized during the financial crisis.<sup>26</sup>

In addition, investors have expressed concern regarding a lack of time to analyze securitization transactions and make investment decisions. Further, market participants have expressed a desire for expanded disclosure relating to the assets underlying securitizations. Investors have complained that the mechanisms for enforcing the representations and warranties contained in securitization transaction documents are weak, and thus are not confident that even strong representations and warranties provide them with adequate protection. In the private market, in many cases, investors did not have the information necessary to understand and properly analyze structured products, such as CDOs, that were sold in transactions in reliance on exemptions from registration. The Commission has taken actions aimed at addressing these concerns.

### Proposed Revisions to Regulation AB

In April 2010, the Commission proposed a number of changes to the offering process, disclosure, and reporting for ABS, which were designed to enhance investor protection in ABS market. The proposals seek to provide investors with timely and sufficient information, including information in and about the private market for ABS, reduce the likelihood of undue reliance on credit ratings, and help restore investor confidence in the representations and warranties regarding the assets. While the Commission historically has not built minimum time periods into its registration process to deliberately slow down the market, based on the assumption that investors can insist on adequate time to analyze securities (and refuse to invest if not provided sufficient time), the proposal included a requirement that the offering documents be available to investors at least five days before an investment decision.

### Dodd-Frank Act Provisions and Other Commission Action

Since Congress enacted the Dodd-Frank Wall Street Reform and Consumer Protection Act (the “Dodd-Frank Act”) in July 2010,<sup>27</sup> the Commission has been active in implementing the provisions related to ABS. In August 2011, the Commission adopted rules in connection with Section 942(a) of the Dodd-Frank Act, which now requires RMBS issuers to continue to provide ongoing disclosure regarding the mortgage pool and other material information regarding the RMBS. Prior to the enactment of this provision, RMBS disclosure was required for only one year or less.

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<sup>26</sup> See, e.g., The PWG March 2008 Report, *supra* note 22, at 2, 8 (noting that the performance of credit rating agencies, particularly their ratings of mortgage-backed securities and other ABS, contributed significantly to the financial crisis).

<sup>27</sup> Pub. L. No. 111–203, 124 Stat. 1376 (July 21, 2010).

The Commission also adopted rules in January 2011 implementing Section 943, on the use of representations and warranties in the market for ABS,<sup>28</sup> and Section 945, which requires an asset-backed issuer in a Securities Act registered transaction to perform a review of the assets underlying the ABS and disclose the nature of such review.<sup>29</sup>

On March 30, 2011, the Commission joined federal banking regulators in issuing for public comment proposed risk retention rules.<sup>30</sup> Section 941 of the Dodd-Frank Act generally requires the rules to: (1) provide that a securitizer must retain not less than five percent of the credit risk of any asset that the securitizer — through the issuance of an ABS — transfers, sells, or conveys to a third party, and (2) prohibit a securitizer from directly or indirectly hedging or otherwise transferring the credit risk that the securitizer is required to retain.<sup>31</sup> Under the proposed rules, a sponsor generally would be permitted to choose from several risk retention options to satisfy its minimum five percent risk retention requirement, which would provide sponsors with flexibility while also ensuring that they actually retain credit risk to align incentives. The proposal also provides a complete exemption from the risk retention requirements for RMBS collateralized solely by “qualified residential mortgages” (or “QRMs”), which is also required by Section 941. The Commission received a number of comments regarding the QRM exemption, which the staff is carefully considering as they move forward with the interagency rulemaking process.

In light of the Dodd-Frank Act and comment received on the April 2010 proposal, in July 2011, the Commission re-proposed the shelf eligibility criteria for offerings of ABS.<sup>32</sup> The Commission also requested additional comment on other aspects of the April 2010 proposal. The Commission received a number of comments on the proposal, and the staff is carefully considering those comments in preparing its recommendations on final rules to the Commission.

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<sup>28</sup> See Disclosure for Asset-Backed Securities Required by Section 943 of the Dodd-Frank Wall Street Reform and Consumer Protection Act, Release No. 33-9175 (Jan. 20, 2011) [76 FR 4489].

<sup>29</sup> See Issuer Review of Assets in Offerings of Asset-Backed Securities, Release No. 33-9176 (Jan. 20, 2011) [76 FR 4231].

<sup>30</sup> See Credit Risk Retention, Release No. 34-64148 (Mar. 30, 2011) [76 FR 24090]. The banking regulators include the Federal Reserve Board, Federal Deposit Insurance Corporation, Office of the Comptroller of the Currency, and, in the case of the securitization of any “residential mortgage asset,” the Federal Housing Finance Agency and Department of Housing and Urban Development.

<sup>31</sup> See § 78o-11(c)(1)(A).

<sup>32</sup> The ABS proposals also implement Section 939A of the Dodd-Frank Act, which requires every Federal agency to review its regulations that require use of credit ratings as an assessment of the credit-worthiness of a security and undertake rulemakings to remove these references and replace them with other standards of credit-worthiness deemed appropriate. Finally, the ABS proposals implement Section 942(b) which requires the Commission to set standards for asset-level disclosure.

Ms. KAPTUR. All right, I thank you.

Thank you, Mr. Chairman.

Mr. CRENSHAW. Thank you.

Chairman White, thank you so much. You have a very impressive background as a prosecutor and in the private sector, and I am sure that that background and experience is going to be useful to you as you undertake this new challenge, and we look forward to working with you to do what we can to make this a better place.

Ms. WHITE. Thank you very much.

Mr. CRENSHAW. Thank you for being here today. This meeting is adjourned.

**Financial Services and General Government Subcommittee**  
**Hearing on the Securities and Exchange Commission**

**Questions for the Record Submitted by Chairman Ander Crenshaw**

*Agency Structure*

**Question:**

**One of the core recommendations out of the Boston Consulting Group Report strongly encouraged a systematic redesign of the Commission, including the overall structure of the Commission and streamlining of the management structure.**

**Right now more than 20 offices report directly to the Chairman—that is a lot of offices. I believe the Commission has done some restructuring within certain offices and divisions, but:**

**In your short time with the Commission, what have you observed about the structure of the agency?**

**Have you considered a more comprehensive overhaul of the agency's structure and divisions?**

**Are there too many levels of management?**

**Response:** Although I have been Chair for only about two months, in that time I have not identified any particular issues with the overall support structure of the agency that I have concluded should be changed. In fact, to date I have been quite impressed with the extensive collaboration and cooperation that the various divisions and offices have shown, both in drafting and developing the rules that impact investors and our markets and in performing the agency's many other duties.

As you know, the responsibilities of the agency are vast. They include implementing and enforcing the federal securities laws, examining thousands of registered entities, reviewing public company disclosures, regulating certain over-the-counter derivative transactions, and overseeing investment and private fund advisers, exchanges, and credit rating agencies, among others. This wide range of duties is handled by five divisions and multiple separate offices specifically tasked with carrying out certain aspects of these important functions. In the past, either the Commission or, in many instances, Congress has seen fit to have the heads of these divisions and offices report directly to the Chair.

As I go forward, I will be considering whether and structural alterations either within or across divisions and offices should be made to make the agency more efficient and effective. I have not at this point considered changing the reporting structure or creating new executive positions to decrease the Chair's direct reports, but will certainly consider and evaluate restructuring options if it becomes necessary to do so.



As the SEC has detailed in its reports to Congress mandated by the Dodd-Frank Act, substantial work has been done over the past several years to analyze and reorganize a number of offices that support the work of the agency, including the Offices of Financial Management, Information Technology, and Human Resources. My understanding is that these changes have improved the efficiency, internal controls, and productivity of these offices.

In addition, the Office of Human Resources (OHR) has worked recently with several Divisions, including the Divisions of Economic and Risk Analysis, Investment Management, and Trading and Markets to assess their organizational structures. These Divisions have evaluated and adjusted their allocation of resources, levels of management, and lines of reporting as appropriate to better carry out their missions. As staff and resources permit, OHR intends to complete a thorough review of the organizational structure of all major Divisions and Offices.

### ***Regional Offices / Leasing***

**Question:** The Boston Consulting Group report, which was required by Dodd-Frank, stated: “The SEC does not currently have a clearly articulated agency-wide strategy for its regional office presence.” In your latest and final report to Congress on the Commission’s progress in implementing the BCG recommendations, I saw that the Commission seems to be looking at regional office operational functions and responsibilities, but there wasn’t specific mention of reviewing the regional office footprints themselves. We mentioned this issue at our hearing with the Commission’s Inspector General and he seemed interested in looking into this.

**Have you discussed your regional office footprint with GSA?**

**Have you discussed closing or merging the Salt Lake City office—or other offices—when those leases come up for renewal?**

**What are your thoughts on the Commission’s regional office footprint?**

**Are the regional offices in the most useful and appropriate places?**

**Response:** The Boston Consulting Group (BCG) report recommended that the SEC analyze its location approach, the balance between – and roles of – regional versus home office staff, and the reporting structure of the regional offices. As was detailed in the October 2012 *Third Report on the Implementation of SEC Organizational Reform Recommendations* (the Third Report)<sup>1</sup>, the Regional Organizational Assessment (ROA) working group was established to assess these recommendations, and a Location Subcommittee was established to undertake a comprehensive assessment of alternative location approaches.

**Regional Office Footprint:** The Location Subcommittee reviewed the footprint of the regional offices. Using the cost-benefit analysis described at page 30 in the Third Report,

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<sup>1</sup> <http://www.sec.gov/news/studies/2012/sec-organizational-reform-recommendations-101712.pdf>

the subcommittee considered closing and consolidating up to five regional offices. On a risk-adjusted basis, none of the potential consolidation options appeared to generate net value to the agency. Critical to the Location Subcommittee's ultimate recommendation against consolidation were several risks and/or disadvantages that would be potentially disruptive to the National Exam and Enforcement programs. These risks/disadvantages included: reduced proximity to stakeholders and important local constituencies if staff presence nationwide was consolidated into fewer offices; increased costs to the agency (primarily from increased leasing and staff travel costs); damage to staff morale/turnover; and decreased talent pool if the SEC's operations were consolidated and the agency lost the ability to attract and retain talented professionals who were unable to relocate.

Based on its review, the Subcommittee concluded that a model of targeted "strategic growth" was the most optimal strategy to follow to ensure efficiency and effective resource allocation. This approach allocates resources to Regional Offices and programs based on evolving needs and priorities rather than on a pro-rata basis.

The Location Subcommittee also recognized that its analysis should be revisited on a periodic basis, as the dynamics of the SEC mission, resources, and workforce change over time.

In my short time at the SEC, I have not become aware of particular issues with our regional office footprint, although I agree with the Location Subcommittee's recommendation that the regional office strategy be revisited on a periodic basis. Going forward, SEC leadership will be making important decisions on how the resources available to the agency should be allocated. Our analysis will include discussions of the advantages and disadvantages of the current regional office footprint, and we will evaluate new options if it appears beneficial to do so.

Discussions with GSA: On August 1, 2011, the SEC entered into a MOU in which the SEC and GSA agreed to collaborate in the development of a comprehensive portfolio strategy that addresses the SEC's current leasehold interests and our future leasing needs. The SEC works with GSA to plan for lease renewals and new leases consistent with the SEC's strategic growth approach and with OMB and GSA leasing policy and practices. GSA staff has been made aware of the BCG recommendations, but to date its input has been limited to the SEC's needs in individual regional offices. As such, although the SEC's leasing staff has had detailed discussions with GSA regarding the footprint of individual regional offices, to date GSA has not offered input or advice concerning alternative location approaches such as decentralization or consolidation of offices.

#### *Settlements with Banks*

**Question: You have an impressive background as a prosecutor and in the private sector. I am interested in how your background as a Federal prosecutor will affect the Commission.**

**Do you intend to encourage the Enforcement Division to go after individuals who were thought to be responsible for the economic collapse of 2007-2008? Is there a statute of limitations for these individuals?**

**Response:** From my experience as a federal prosecutor, I expect to bring to bear my experience and resolve to aggressively pursue those who violate our federal securities laws, including those individuals where there is evidence of wrongdoing during the financial crisis in 2007-2008 to the extent that any such cases would not be barred by the applicable statute of limitations.

That said, I believe that the SEC has a strong record of cases holding accountable those institutions and individuals who engaged in misconduct related to the financial crisis. To date, the SEC has filed crisis-related actions against 157 entities and individuals, including more than 65 CEOs, CFOs, and other senior corporate officers at some of Wall Street's most sophisticated banks and institutions, including Goldman Sachs, J.P. Morgan, Citigroup, Wachovia, Wells Fargo, Bank of America, Bear Stearns, Fannie Mae, Freddie Mac, Countrywide, New Century Mortgage, and other large financial firms. These actions have resulted in \$2.68 billion in total penalties, disgorgement and other monetary relief for investors.

While I am proud of the agency's record, those metrics alone cannot adequately capture the complexity and sophistication of the transactions and products involved in the agency's financial crisis-related cases. Our ability to harness the expertise of our enforcement staff, including through recently-created specialized units and the deep experience of recently-hired industry experts, has been and will continue to be critical to our success in this area.

Although I cannot comment on the specifics on any particular investigation, we generally expect that any remaining financial crisis-related investigations will be resolved in the near term. We have pursued all of our crisis-related investigations with vigor and, as in all of our investigations, are mindful of any statute of limitations deadlines tied to the facts of any particular investigation.

**Question: Is there any truth to the idea of "too big to jail"?**

**Response:** Although the SEC lacks the ability to jail violators, at the SEC there is no institution that is too big to charge. The Commission considers a number of factors when determining the appropriateness of a particular penalty sought or imposed in its enforcement actions, but has no policy or practice constraining its ability to file to seek or impose a particular penalty or other relief because of any real or perceived broader economic impact.

**Question: Recently, Federal judges have been critical of SEC settlements.**

**Is there a metric that the Commission uses in determining whether to go to trial or not?**

**Response:** The Commission is rigorous and methodical in analyzing each offer to settle an enforcement action. Every settlement offer is analyzed on a case-by-case basis in light of the unique facts and circumstances of that specific case. In each case, the Division of Enforcement and the Commission analyze whether a proposed settlement advances the public interest by obtaining the relief that we could reasonably expect to receive at trial, without assuming the risks and costs of lengthy and protracted litigation. It is also worth noting that our settlements achieve a significant measure of accountability and deterrence because of the detailed factual allegations and findings contained in our complaints, orders instituting proceedings, and settlement documents – factual allegations or findings that present a virtual road map of the wrongdoing that the Commission contends violated the federal securities laws. In addition, the very public nature of our settlements enhances their deterrent impact – our settlements frequently are accompanied by press releases, dissected by the media, analyzed in detail by the financial industry and the defense bar in various public forums, and are the subject of speeches and other public statements by the Chair, the Commissioners, and other SEC officials.

There is economic research that indicates that SEC settlements have consequences for firms as well as management and directors. For instance, a group of economists found that the reputational penalties to a firm of an SEC enforcement action for financial fraud are highly significant: for each dollar that a firm misleadingly inflates its market value, on average, it loses both this dollar plus an additional \$3.08 when its misconducts is revealed (Jonathan M. Karpoff, D. Scott Lee & Gerald S. Martin, *The Cost to Firms of Cooking the Books*, 43 Journal of Financial and Quantitative Analysis, 2008). The same economists studied 2,206 individuals identified as responsible parties for 788 SEC and Department of Justice enforcement actions for financial misrepresentation from 1978 through mid-2006. They found that 93% of the individuals lose their jobs by the end of the regulatory enforcement period, with the majority being fired (Karpoff, Lee & Martin, *The Consequences to Managers for Financial Misrepresentation*, 88 Journal of Financial Economics, 2008).

**Question: Do you believe the fines the SEC agreed to in recent settlements are a big enough deterrent for recidivist institutions?**

**Response:** As indicated above, I believe that our settlements have strong deterrent impact for a number of reasons, including because they achieve penalties and relief that approximates what we could achieve at trial, and because we can achieve those results closer in time to the actual misconduct – rather than after years of protected litigation where the passage of time may minimize the deterrent impact.

With respect to recidivist institutions, the Commission is, at times, confronted with entities or individuals that have repeatedly violated the federal securities laws. In some instances, such defendants' subsequent misconduct violates both the federal securities laws and a federal court injunction or bar previously obtained by the Commission. While we make full use of our existing penalty authority, the SEC's ability to impose penalties

in its settlements or seek penalties in federal district court actions is explicitly limited by certain statutory caps. As such, I believe current law does not provide the Commission with sufficient authority to impose a specific penalty enhancement to deter this category of determined recidivist violators. Former SEC Chairman Mary Schapiro requested two statutory changes that would provide new sources of penalty authority to explicitly increase the punishment of repeat offenses, and I support those statutory requests, namely:

- The Commission should be authorized to seek a penalty enhancement equal to three times the otherwise applicable penalty cap if within the preceding five years a defendant has been criminally convicted for securities fraud or become subject to a judgment or order imposing monetary, equitable, or administrative relief in any SEC action alleging fraud. This would enable the Commission to seek monetary penalties against recidivists that are over-and-above the limitations described previously, regardless of the calculation method used.
- The Commission should be authorized to seek a civil penalty if an individual or entity has violated an existing federal court injunction or a bar obtained or imposed by the Commission.

**Question: How does the fact that a number of the Commission's high profile settlements have been thrown out in court affect the SEC's position in negotiating future settlements on behalf of investors?**

**Response:** Certain press reports and commentary have expressed a level of dissatisfaction with the penalties obtained by the SEC in specific high profile settlements. Such commentators often compare SEC penalty amounts in proposed settlements with investor loss amounts, asserting that the gulf between the two is evidence of the low impact of the SEC's sanction in a particular case. That commentary often does not account for the fact that the SEC does not currently have the statutory authority to seek a penalty that is calculated based on investor loss (i.e., it is not a restitutionary or compensatory penalty scheme).

I support statutory changes requested by former Chairman Schapiro that would enhance the impact of the Commission's settlements in this regard. Specifically, I support a statutory change that would authorize a penalty calculation method based on the amount of "investor losses" incurred as a result of a defendant's violation to be available in both civil and administrative actions. This would allow the Commission to take into account more directly the harm inflicted on investors in seeking appropriate penalties.

That said, even in the absence of this enhanced penalty authority, I do not think the fact that a small number of federal judges have raised questions about a very small number of our proposed settlements impacts our ability to negotiate future settlements. While additional authority to explicitly factor in investor losses tied to a violation would enhance our negotiating position to some extent, the well-established and above-

described ways in which our settlements have real impact and achieve real accountability ensures that our settlement negotiations are treated with the appropriate level of seriousness by all parties.

**Question:** Do you think defendants assume that in the end the SEC will settle rather than go to trial?

**Response:** I do not believe so. The SEC is fully prepared to go to trial every time we bring an enforcement action. That said, as a general matter we do not delay justice and relief for investors when we can obtain through a settlement the relief that we could reasonably expect to receive at trial, without the delay of a lengthy and protracted litigation. As indicated above, I believe SEC settlements achieve a significant measure of accountability and deterrence because of the detailed factual allegations contained in our complaints and settlement documents and by the very public nature of the discussion of our settlements by the industry, the defense bar, and the press.

The reality is, as trial-ready as we may be, Wall Street banks and other large public companies often weigh the risks of litigating to trial against the SEC – including the risk of loss, litigation costs, reputational damage and other factors – and choose instead to offer a proposed settlement. On the other hand, individuals may weigh the risks of litigating against the SEC differently than do large banks and public companies, particularly given that our settlements often include remedies such as industry bars that restrict an individual's ability to earn a living in the financial industry. Seventy percent of the financial crisis-related cases we have brought against individuals were filed as contested actions. It is to be expected that defendants will analyze these factors differently, according to their own unique circumstances and given their particular assessment of the estimated impact of an SEC enforcement action.

**Question:**

**Previous Chairmen have pointed to a lack of resources as one of the reasons for not going to trial.**

**Please explain to this Committee how your FY 14 budget request will help address this issue.**

**Can you tell us how your background will directly affect the Commission and its priorities for the coming year?**

**Response:** A strong and aggressive litigation function is essential to the agency's success. As a former U.S. Attorney, I know firsthand the deterrent value that comes from having vigorous litigators that are ready, willing, and able to go to trial to hold wrongdoers accountable for their misconduct. Securities laws violators can never be allowed to labor under the misimpression that the SEC is afraid or unwilling to litigate or otherwise would rather settle than litigate its cases. As Chair, I am committed to fielding and resourcing the strongest trial unit possible. Under my leadership, the SEC will be

prepared to litigate all cases that should or do go to trial, including cases where proposed settlement terms are unsatisfactory or unwarranted.

The agency's fiscal year 2014 budget request recognizes the critical role that the Enforcement Division's trial unit plays at the SEC. Our biggest resource need in this area centers around the ability to hire additional trial attorneys to handle an increasing number of litigated matters. In addition, the cases being prosecuted by the SEC are of increasing complexity, requiring the hiring of additional expert consultants and expert witnesses. The increased resources we have requested for our litigation function will strengthen our ability to assemble and present strong cases at trial in order to secure outcomes that appropriately punish misconduct and achieve justice and relief for investors.

### *High Frequency Trading / Dark Pools*

**Question:**

**High frequency traders are continuing to affect the markets. As high frequency trading, dark pools and other emerging market trends become a bigger and bigger part of our markets, I am interested to know how the SEC plans to keep up with these changes.**

**Does the SEC have enough market experts to understand these types of emerging market trends to appropriately react to them?**

**Response:** The SEC has taken important steps to upgrade its institutional capabilities for understanding emerging market trends, both by enhancing its data resources and by hiring market experts to analyze and use the data. It adopted a Large Trader Reporting Rule that expands available information about the most active traders in the markets. It approved a Consolidated Audit Trail Rule that directs the SROs to submit a plan for a facility that, when implemented, will greatly enhance the ability of the SEC and SROs to surveil the markets and enforce trading rules. In addition, the SEC has implemented a new system (MIDAS) to collect and analyze market data from both the consolidated data feeds and the "proprietary" data feeds offered by the exchanges to their customers. MIDAS will enable visibility into every exchange execution and displayed order, modification, and cancellation.

To use all of these new data tools effectively, the SEC has hired a number of additional personnel with quantitative and trading expertise. They are located throughout the agency, including the Division of Economic and Risk Analysis, the Office of Analytics and Research in the Division of Trading and Markets, and within the Market Abuse Unit in the Division of Enforcement. Although the Commission has made substantial progress in this regard, we are continuing to prioritize the hiring of staff with practical market experience and expertise to make sure we stay on top of emerging market trends.

**Question: Within the increase in funding you have requested in FY 2014, is any of it directed at monitoring high frequency trades?**

**Response:** In FY 2014, the Division of Trading and Markets is requesting 10 new positions to undertake its new market-related responsibilities under the Dodd-Frank Act, as well as continuing challenges in the area of market supervision. The responsibilities of at least four of the new staff would include monitoring developments and issues in the exchange and over-the-counter markets for securities, including market structure developments such as the growth of high-frequency trading and dark liquidity, as well as the potential for excessive market volatility.

**Question: What is the status of the Commission's development of a consolidated audit trail? Would this be a real time audit?**

**Response:** The Commission adopted Rule 613 in July 2012 to create a comprehensive consolidated audit trail that would allow regulators to efficiently and accurately track all activity throughout the U.S. markets in National Market System (NMS) securities. Among other things, the rule requires the self-regulatory organizations (SROs) to jointly submit a plan to create, implement and maintain a consolidated audit trail. The rule specifies the type of data to be collected and when the data is to be reported to a central repository.

The SROs currently are developing the plan to be submitted to the Commission in accordance with Rule 613 by December 6, 2013. The SROs have made available a wide range of information about their process for developing the NMS plan and the current status of those efforts at [www.catnmsplan.com](http://www.catnmsplan.com). Rule 613 provides that the NMS plan must require that most audit trail data be reported to a central repository by 8:00 a.m. Eastern Time the following trading day – and be subsequently available to regulators for analysis.

**Question: How do you see the SEC monitoring these types of trades going forward?**

**Response:** As noted above, the SEC adopted the Large Trader Reporting Rule and plans to implement and use the large trader reporting system as a mechanism to assist in improving oversight of the markets. Also, the Consolidated Audit Trail Rule will enhance the ability of the SEC to monitor the markets and enforce trading rules. Further, quantitative and trading experts in the Division of Economic and Risk Analysis, the Office of Analytics and Research in the Division of Trading and Markets, and the Market Abuse unit in the Division of Enforcement will be utilizing the MIDAS system described above and other information sources to observe and examine trading activity, including exchange execution and displayed orders, modifications, and cancellations by high frequency traders.

**Question: How does the SEC work with Treasury's Office of Financial Research, which is also monitoring markets and trades?**



**Response:** Staff of the SEC shares financial-related data with the OFR. For example, staff provides OFR the money market fund portfolio holdings data from Form N-MFP. In addition, OFR receives private fund data filed on Form PF in order to assist the Financial Stability Oversight Council in its assessment of systemic risk, consistent with section 404 of the Dodd-Frank Act. SEC staff also coordinates with OFR through the Financial Stability Oversight Council's Data Committee and has coordinated on launching the international Legal Entity Identifier project through its participation on the Regulatory Oversight Committee, which is chaired by OFR staff.

### *Social Media*

**Question:**

Social media is increasingly more integral to how companies operate. The SEC recently released a staff report on the SEC's investigation into Netflix's CEO and his disclosure of Netflix streaming 1 billion hours on his personal Facebook page. The staff report did not find any wrongdoing by the CEO; however, the report did expand on SEC guidance from 2008 and noted that "every case must be evaluated on its own facts". This is not very clear guidance in an area that is becoming more and more significant. Further, this guidance is from SEC staff, not the Commission.

**Is this issue something the Commission plans to discuss and issue guidance on?**

**Is it appropriate for SEC staff to be setting policy through staff-issued reports when these reports can have wide ranging effects?**

**Is guidance issued by SEC staff in staff report reviewed by the Commission first?**

**Are there areas for improvement in this area to be sure staff-issued guidance does not set Commission policy and reflects the Commission's views?**

**Response:** The "Netflix Report" is a Report of Investigation issued pursuant to Section 21(a) of the Exchange Act that expresses the views of the Commission itself, not the staff.<sup>2</sup> Section 21(a) of the Exchange Act authorizes the Commission to investigate violations of the federal securities laws and, in its discretion, to publish information concerning any violations. On occasion, the Commission may deem it appropriate and in the public interest to issue a Section 21(a) report to provide its views on an issue or concern that was considered during the course of an investigation.

The Commission issued the Netflix Report in response to possible confusion in the marketplace and questions that arose following the significant media coverage of the Netflix investigation. The questions surrounded the application of Regulation FD to the use of social media channels such as Facebook. (Regulation FD was adopted in 2000 to address concerns about selective disclosure by public companies of material, non-public information.)

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<sup>2</sup> The Report can be viewed at <http://www.sec.gov/litigation/investreport/34-69279.pdf>.

The Commission concluded that it was important to clarify how companies could make disclosures through social media in a way that would comply with Regulation FD and the Commission's 2008 guidance on the use of corporate websites. The Netflix Report states that if a company wants to use a social media channel to disseminate material information, it should alert investors and the market of its intention to do so. Companies would need to consider the steps taken to alert investors and the market about which communication channels the company intends to use and the types of information that may be disclosed using those channels.

As a result of the issuance of the Netflix Report, I believe that there is greater clarity for those companies that may want to use Facebook, Twitter, or other social media sites to communicate with shareholders and the market. Therefore, I do not currently anticipate the Commission will issue additional guidance on this topic, but will monitor these issues going forward.

*Waste within Trading and Markets / Internal Controls*

**Question:**

**I was disappointed to hear of the waste within the Division of Trading and Markets with regard to their procurement of unnecessary computer equipment and software. I understand the Inspector General's office is currently completing a follow-up to review the Commission's response to the IG's recommendations.**

**Can you tell us whether reforms have been implemented within the Trading and Markets Division?**

**Are the reforms applicable agency-wide?**

**Have you discussed implementing more internal controls related to procurement within other divisions at SEC?**

**Response:** The conduct described in the IG's report regarding the Automated Review Program was clearly unacceptable. There are now a number of reforms in place to prevent the problematic activity surrounding procurement of computer equipment and software from happening again.

With respect to the Division of Trading and Markets (TM) specifically, the Division brought in new leadership for the Automation Review Policy (ARP) program and enhanced its policies and procedures. TM management also took personnel actions with regard to the implicated ARP staff.

On March 26, 2013, the Office of the Inspector General (OIG) concluded that the steps taken within TM to meet the intent of OIG's recommendation regarding monitoring of ARP equipment purchases were adequate. The recommendation was closed as of that date.

In addition to its actions specific to the ARP program, the SEC has, over the past several years, implemented a complete overhaul of its IT procurement program. The reforms and internal controls implemented by the Office of Information Technology (OIT) and the Office of Acquisitions have enhanced the governance and security of the procurement process. Each office and division within the agency must take part in the SEC's capital planning and investment control (CPIC) process for IT procurement:

- Procurement requests that are significant in scope or involve new technology are reviewed first at the Division or Office level by the Division Information Officer (DIO), an OIT employee who is assigned to the Division or Office to manage its IT needs and act as a liaison on its behalf. After a procurement request has been approved by management of the initiating Office or Division, the request must be sent to the office of the Chief Technology Officer (CTO) in OIT.
- The CTO's Office reviews each request. If the request is for existing technology, the CTO's Office may act on the request. Requests which are new to the technology environment or which involve a significant expenditure are referred to The Project Review Board (PRB).
- The PRB is chaired by the CTO. Voting members include the Chief Information Security Officer from OIT, the Assistant Director for Business Management from OIT, the Assistant Director for Planning and Budget from the Office of Financial Management (OFM), and the Chief of the IT Support Branch from the Office of Acquisitions (OA). The participation of OIT, OFM, and OA ensures that all procurements are approved consistent with the Clinger-Cohen Act's requirement that each agency establish "a process for maximizing the value and assessing and managing the risks of information technology acquisitions."
- Upon request from any member of the PRB, OIT's Technology Review Board evaluates a proposed procurement to ensure that it is cost effective, will meet the Agency's technical needs and business objectives, and can be supported by the SEC's systems and implemented and used as intended by the SEC's staff.

Furthermore, the Office of Acquisitions has implemented a number of additional checks to ensure that all technology acquisitions have been properly reviewed and approved:

- All contract funding requests, approvals, and obligations (except for certain limited purchases for \$3000 or less) are now in a single, automated procurement system (PRISM), which enables OA operational managers to view relevant documents and processes for these requisitions.
- The Acquisition Requisitions Management System is a SharePoint site that provides an additional opportunity for OA managers to check and properly assign all procurement requests.

- All requisitions for IT hardware, software, and services must be reviewed by OA contracting staff to verify OIT engagement in the requirement.
- OA has initiated a Contract Review Board for all procurement actions over \$650K. All OA managers understand that procurements for IT products and services must have OIT engagement, including review through the CPIC process.

The SEC believes that its IT procurement processes are well-controlled and are consistent with industry standards. The SEC is committed to ongoing review of the CPIC and acquisition processes to ensure that opportunities for improvement are identified and acted upon.

## **Questions for the Record Submitted by Congressman Kevin Yoder**

### ***Procedures to Protect***

**Question:** What procedures are in place to ensure SEC subpoenas for electronic communications comply fully with constitutional, statutory, and common law protections including the Fourth Amendment right to be free from unreasonable searches and seizures and the right to due process and protection against self-incrimination?

**Response:** The Commission and staff take very seriously our obligations to comply with the law, including constitutional, statutory, and common law protections available to persons from whom we seek information. Our Division of Enforcement works closely with the Office of General Counsel to monitor legal developments and provides guidance to our staff on appropriate practices, including with respect to the Electronic Communications Privacy Act (ECPA). Beyond this, we make available to the public on our website a copy of the Division's Enforcement Manual (<http://www.sec.gov/divisions/enforce/enforcementmanual.pdf>), which describes a number of our policies and practices. We also routinely provide a notice to persons who are asked to supply information to us either voluntarily or pursuant to subpoena that describes the uses we make of the information and certain rights they have in responding to our requests (<http://www.sec.gov/about/forms/sec1662.pdf>).

### ***Retention***

**Question:** What procedures are in place to limit the retention of electronic communications not directly relevant to a lawful investigation?

**Response:** The Commission is subject to records retention schedules approved by the National Archives and Records Administration. Pursuant to the records schedule applicable to Enforcement investigative case files, electronic communications produced by third-parties are not required to be retained beyond the closing of the matter unless they were used as exhibits in investigative testimony, used in public enforcement proceedings, or are otherwise viewed as key documents concerning the matter. See Enforcement Records Schedule, [http://www.archives.gov/records-mgmt/rcs/schedules/independent-agencies/rg-0266/n1-266-09-004\\_sfl15.pdf](http://www.archives.gov/records-mgmt/rcs/schedules/independent-agencies/rg-0266/n1-266-09-004_sfl15.pdf). Electronic communications that are not relevant to an investigation are not required to be retained after the matter is closed.

### ***Minimization***

**Question:** What procedures are in place to ensure SEC requests to 3<sup>rd</sup> party service providers for electronic communications are limited to the receipt of information that not privileged?

**Response:** I understand that when the Commission has issued subpoenas to ISPs, the Commission, as required by Section 2703(b)(1)(B) of the ECPA, has in the ordinary course provided notice of such subpoenas to the subscriber or customer of the ISP. Providing notice in this manner mitigates potential privilege concerns. To the extent that the subscriber or customer believes that the e-mail contents may be privileged, the subscriber or customer was able to (and did) raise objections to the production of the information. In those instances, Commission staff would routinely work with the ISP and the subscriber or customer to address the issue.

### *Trade Secrets*

**Question: What procedures are in place to ensure SEC requests to 3<sup>rd</sup> party service providers for electronic communications are limited to the receipt of information do not contain trade secrets?**

**Response:** As noted above, when the Commission has issued subpoenas to ISPs, the Commission has in the ordinary course provided notice of such subpoenas to the subscriber or customer of the ISP. To the extent the subscriber or customer believes that the e-mail contents may include trade secret information that is not relevant to the Commission's investigation, the subscriber or customer was able to (and did) raise the issue. In those instances, the Commission staff would routinely work with the ISP and the subscriber or customer to address the issue. To the extent that trade secret information is relevant to the Commission's investigation, there is no legal basis on which a subscriber or customer can object to the production of such information. The scope of the Commission's investigative authority is defined by statute and judicial interpretation. *See, e.g.,* 15 U.S.C. § 78u(b); *SEC v. Jerry T. O'Brien, Inc.*, 467 U.S. 739, 741, 743-44 (1984).

### *Asserting Rights*

**Question: How can the target of investigation assert any of their rights if they are not aware that the SEC is accessing their information by going directly to a 3<sup>rd</sup>-party service provider, without any notice to the target?**

**Response:** As noted above, when the Commission has issued subpoenas to ISPs, the Commission has in the ordinary course provided notice of such subpoenas to the subscriber or customer of the ISP.

### *Warshak Decision*

**Question: After the *Warshak* decision in 2010, how many times has the SEC used its subpoena authority to compel a 3<sup>rd</sup> party service provider to disclose the contents of electronic communications?**

**Response:** Staff informs me that the SEC does not maintain statistics on the particular types of persons or entities subpoenaed; however, *Warshak* has greatly impeded the SEC's ability to serve administrative subpoenas on ISPs absent the consent of the subscriber.

**Question:** Right now under ECPA the SEC is barred from accessing email for 180 days. As a result of *US v. Warshak*, many companies are requiring a warrant at all times.

**How does the SEC handle these existing barriers to accessing emails?**

**Response:** The *Warshak* decision has impeded the Commission's ability to serve administrative subpoenas on ISPs absent the consent of the subscriber or customer, and in a number of cases has effectively foreclosed the Commission from obtaining access to crucial evidence directly from ISPs absent consent of the person or entity that is being investigated. The Commission can still subpoena the information directly from the person under investigation; however, in many cases that is not an effective alternative. Unlike agencies with criminal jurisdiction, the Commission does not currently have authority to obtain criminal warrants to compel production of evidence from ISPs that would corroborate, refute or supplement information provided by the customer.

The Commission cannot rely on the Department of Justice (DOJ) to obtain search warrants in this context. DOJ only has authority to seek search warrants to advance its own investigations, not SEC investigations. Thus, the Commission cannot request that the DOJ apply for a search warrant on the SEC's behalf. Additionally, many SEC investigations of potential civil securities law violations do not involve a parallel criminal investigation, and thus there is no practical potential avenue for a search warrant being sought in those cases.

**Question:** What tools are available to the SEC to preserve evidence and access records directly from subject of investigation using a subpoena? What tools are available to courts to enforce SEC subpoenas when subpoenaed materials are destroyed or the subject of the investigation refuses to turn them over?

**Response:** In carrying out our mandate to investigate violations of the federal securities laws, the Commission frequently seeks to obtain information, including the contents of e-mail and other electronic communications. Such communications can provide direct and powerful evidence of wrongdoing. We often seek production of such communications from persons whose conduct we are investigating – typically either by administrative subpoena or, for certain regulated entities, pursuant to specific statutory rights of access. However, because persons who violate the law frequently do not retain copies of incriminating e-mail communications, or choose not to provide e-mails in response to Commission subpoenas, we previously have sought the contents of electronic communications directly from internet service providers (ISPs). Although the Commission can still subpoena the information directly from the person under investigation, in many cases that is not an effective alternative, as unfortunately, individual account holders sometimes delete responsive e-mails, or fail to produce them, notwithstanding subpoenas that call for their production. Enforcement staff's experience is that subpoenas to individuals can be more effective if the subpoena recipient knows the Commission has the ability to go to an ISP and test whether they have fully responded to a subpoena. In general, a subpoena enforcement

action in federal court is not an effective alternative because it is a lengthy process that slows down the investigation and ultimately does not address the problems posed by deletion within or spoliation of an individual's email account. Without the ability to obtain from the ISP independent, objective evidence that the subscriber or customer has failed to produce responsive information, we are hampered in challenging even a false claim that the subpoena has been complied with.

**Question: In your letter to Senator Leahy, you contend that the *Warshak* opinion has "greatly impeded the SEC's ability to serve administrative subpoenas on ISPs absent the consent of the subscriber."**

**Does the SEC have any objective data, studies, reports, or other evidence to demonstrate that its mission has been greatly impeded by the *Warshak* case?**

**Response:** Although Commission staff is not aware of specific data, studies, or reports that consider the impact of the *Warshak* decision, I understand from staff that the decision has in fact prevented the Commission from obtaining evidence of securities law violations, as well as evidence that would independently verify the veracity of the information provided to the Commission by customers or subscribers being investigated for securities laws violations. Results such as this significantly impede the agency's ability to protect investors and enforce the securities laws. I am not aware of a metric that would quantify these negative impacts.

**Question: Is the SEC's normal protocol to bypass the targets of civil investigations and go directly to service providers that are covered under ECPA?**

**Response:** No. The SEC routinely seeks production of communications directly from persons whose conduct we are investigating.

**Question: Given the significant problems ostensibly created by *Warshak*, which was decided in December 2010, can you direct me to public requests (e.g. in written or oral testimony) where the SEC has asked its Congressional Committees for the statutory authority it is now seeking?**

**Response:** The Commission requested a mechanism be included in the ECPA to enable a federal civil agency to obtain electronic communications from an ISP for use in a civil enforcement investigation upon satisfying a judicial standard comparable to the one that governs receipt of a criminal warrant in a May 15, 2013 letter to the Chairmen of the Senate Committee on Banking, Housing and Urban Affairs and the House Committee on Financial Services. That request was part of a group of draft legislative proposals provided to the Chairmen of those committees. I requested a similar draft legislative provision in a letter dated April 24, 2013 to the Chairman of the Senate Committee on the Judiciary. To my knowledge, no such previous requests were made.



**Question:** If the SEC's problem in this regard preceded the legislative push to update ECPA and began with *Warshak*, why hasn't the agency made a more concerted effort to obtain the civil warrant authority it is now seeking?

**Response:** The above described legislative proposal, designed to address the issues created by *Warshak*, was included in the first set of Commission-approved legislative proposals sent to Congress since the Sixth Circuit's decision.

### *Process for Limiting Overbreadth*

**Question:** Unlike criminal law enforcement agencies, the SEC has a broader authority under the regulatory "power of inquisition," which the Supreme Court has said, "is not derived from the judicial function. It is more analogous to the Grand Jury, which does not depend on a case or controversy for power to get evidence, but can investigate merely on suspicion that the law is being violated, or even just because it wants assurance that it is not. When investigative and accusatory duties are delegated by statute to an administrative body, it, too, may take steps to inform itself as to whether there is probable violation of the law." [U.S. v. Morton Salt, 338 U.S. 632, 642-43 (1950)].

**Given that the SEC has a much broader investigative authority, how does the SEC intend to limit its email searches?**

**Response:** As an initial matter and from my experience as a federal prosecutor, I do not believe that the Commission has much broader investigative authority than the federal criminal authorities. Specifically, the scope of conduct subject to criminal investigation – the entire federal criminal code – is significantly broader than the Commission's investigative jurisdiction, which is focused on potential violations of the federal securities laws. Beyond this, in the *Morton Salt* decision, which involved the FTC, the scope of the FTC's investigative authority was described as "analogous" to that of the grand jury, which is the primary investigative mechanism in the criminal context. See *United States v. Morton Salt Co.*, 338 U.S. 632, 642 (1950) (administrative investigative authority "is more analogous to the Grand Jury, which . . . can investigate merely on suspicion that the law is being violated"). Unlike the criminal authorities, for example, the Commission does not currently have the power to obtain search warrants to search emails.

With respect to using the Commission's subpoena powers, the SEC only issues subpoenas when an investigation has been initiated. Investigations are initiated based on whether, and to what extent, the investigation has the potential to address conduct that violates the federal securities laws. Threshold issues considered when evaluating the facts include an analysis of whether the facts suggest a possible violation of the federal securities laws involving fraud or other serious misconduct. Once an investigation has begun, we endeavor to seek evidence that is relevant or material to our investigations.

*Limiting Civil Authority Increases*

**Question:** The SEC wrote a letter to the Judiciary on April 24, 2013 requesting that the ECPA amendments include a provision that would allow a governmental entity to subpoena electronic communications from an ISP provided it obtains an order for such disclosure from any court of competent jurisdiction upon a finding of probable cause, supported by oath or affirmation, to believe that evidence of a civil violation of federal law will be found in a wire or electronic communication. The current bill would only allow such disclosure with probable cause that a criminal violation has occurred.

**Given the large number federal, state and local administrative agencies with subpoena power, is there any meaningful way to differentiate the authority the SEC seeks for civil investigations from the civil investigatory interests of these other agencies?**

**Response:** While I cannot speak to other agencies investigatory or legislative needs, I believe that the modest change suggested in the Commission's May 15 letter including legislative proposals would better permit the SEC to protect investors, assist victims of securities fraud, and hold accountable those who violate our federal securities laws while at the same time preserving the privacy objections the underlying bill is seeking to address. What we suggested would involve a judicial finding of probable cause before such records could be obtained.

*Keeping Civil Evidence Separate from Criminal Evidence*

**Question:** Form 1662 of the Securities and Exchange Commission, (<http://www.sec.gov/about/forms/sec1662.pdf>) is designed to be used with all SEC civil subpoenas. It expressly states:

**"The Commission often makes its files available to other governmental agencies, particularly United States Attorneys and state prosecutors. There is a likelihood that information supplied by you will be made available to such agencies where appropriate. Whether or not the Commission makes its files available to other governmental agencies is, in general, a confidential matter between the Commission and such other governmental agencies."**

**Given this reality will the SEC be able to keep civil investigatory material separate from criminal matters?**

**Response:** The Commission's enforcement investigations are non-public and confidential, and information obtained by the Commission during its investigations is treated as such. The Commission has extensive experience in maintaining the confidentiality of highly-sensitive, market-moving information. While the Commission does not have criminal authority, when the Commission shares information with the Department of Justice – as the law specifically provides for (*see* 15 U.S.C. § 78u(d)(1)) –

it does so pursuant to appropriate assurances that the information will be treated confidentially.

**Questions for the Record Submitted by Congressman Steve Womack**

*Sequestration*

**Question:** The Office of Management and Budget (OMB) has determined that sequestration should apply to three private entities which do not receive appropriated funds: the Financial Accounting Standards Board (FASB), the Public Company Accounting Oversight Board (PCAOB), and the Securities Investor Protection Corporation (SIPC). On December 5, 2012, the House Committee on Financial Services sent a letter to the House Appropriations Committee, asking it to include a provision in the appropriate legislative vehicle to clarify that these entities are not subject to sequestration.

**Does the SEC have an opinion on this issue?**

**Response:** OMB has made the determination that the PCAOB, FASB, and SIPC funds are subject to sequestration under the Budget Control Act of 2011. Over the last several months, SEC staff have consulted with OMB and the three named organizations to make sure the current law with respect to sequestration is implemented appropriately.

The Commission has not taken a position about any potential legislation exempting these organizations from sequestration. However, my view is sequestration can hinder their ability to carry out their important missions for the benefit of the investing public. So I would be pleased to support a legislative proposal to exempt these organizations from sequestration.

**Questions for the Record Submitted by Congresswoman Jaime Herrera Beutler**

*SEC and Department of Labor Fiduciary Standards*

**Question:** The SEC recently issued an information request on a possible fiduciary standard for broker-dealers pursuant to Dodd-Frank. The Department of Labor has also been working on a reproposal of its fiduciary standard of care for retirement plans and IRAs. The SEC and DOL have made it clear that their rules will not be uniform. Consequently, an investor seeking help with a regular brokerage account and an IRA will be subject to two entirely different rules.

**What are your thoughts on the creation of two separate regimes, in light of one of the goals of Dodd-Frank Section 913 was to minimize investor confusion?**

The SEC and DOL seem to be working on different schedules. This will likely mean that the brokerage industry will have to be restructured twice in the course of a few years – once to conform to the DOL rules and second time to conform to the SEC rules.

**How does this make sense?**

**Won't this cause significant costs that investors will eventually have to bear?**

**Response:** I appreciate the concerns you raise about the interplay between potential fiduciary rulemaking by the SEC and that of the Department of Labor (DOL). As you note, the SEC has issued an information request regarding a possible uniform fiduciary standard for broker-dealers and investment advisers. The comment period for the request for information ends in early July 2013.

The Commission made clear in its release that it has not yet determined whether or not to propose a uniform fiduciary duty for broker-dealers and investment advisers.

However, I am aware of and focused on the prospect of the DOL redefining the fiduciary duty standards for IRA accounts, where broker-dealers routinely interact with retail investors, and how such standards may interact with any fiduciary standard for broker-dealers that the Commission may implement. Certainly, each agency has a different statutory mandate, but I am sensitive to imposing unnecessary costs to investors and to the industry.

Since the DOL's proposal in 2010, SEC staff have coordinated, and continue to coordinate, with DOL staff on the question of how to implement a fiduciary standard and the practical effect for financial services providers – particularly broker-dealers – of operating under a fiduciary standard of conduct, as well as any impact it may have on retail investors.

Of course, ultimately, the DOL has its jurisdiction and statutory authority. My goal and that of SEC staff is to continue to work together to coordinate our rules as much as possible and appropriate under our different statutory standards, with the goal of protecting investors without imposing unnecessary or burdensome costs on industry.

**Questions for the Record Submitted by Ranking Member José Serrano**

*Staffing*

**Question:** The President's budget request of \$1.674 billion will support 676 new positions. The testimony points to the new responsibilities of the SEC and the fact that the agency needs to hire experts in various fields to properly oversee the constantly evolving financial markets.

**What would the impact be of not augmenting those core functions with expert staff?  
As we all know, it can be difficult to hire quickly in the federal government.**

**Response:** The 676 new positions are necessary to fully implement programs to oversee areas such as over-the-counter derivatives, private fund advisors, and clearing agencies, among others. Specifically, we would not have the staff we need for:

- Enforcement investigations and litigation, especially in light of new SEC responsibility areas;
- Examinations and oversight of hedge fund advisers and other investment advisers;
- Examinations and oversight of clearing agencies;
- Expanded oversight of exchange-traded funds;
- Economic analysis for rulemaking and risk assessment related to new registrants, such as hedge funds and derivatives market participants; and
- Further buildout of the agency's examinations of credit rating agencies.

**Question:** If the SEC is successful in securing the President's request for fiscal year 2014, how confident are you that you will be able to fill these new positions with the types of experts you need?

**Response:** We believe we would fulfill our hiring goals. We have invested in streamlining our hiring processes and developed more strategic approaches to filling our vacancies. We would also add resources in our recruiting and staffing functions to enable us to carry out the hiring.

Specifically, we use an agency specific hiring authority for our core mission related positions that streamlines the hiring process. The Excepted Service Hiring Authority (ESHA) allows us to go outside of the normal competitive process (while preserving veteran's preference) to fill our mission critical skills. For ESHA positions, we have developed a targeted recruitment strategy to more precisely and quickly locate individuals who possess the requisite skills and expertise that we require. If granted the requested positions, we would dedicate additional resources to enhancing our recruitment team in order to attract the best qualified candidates.

Additionally, we have made significant strides in developing pipelines through our student programs. The programs are used to locate, identify, and capture fresh talent. As an example, the 2013 summer session of the Student Volunteer Program garnered 5000

applicants. Obviously, we are administratively unable to provide opportunities for those vast numbers, but it shows the great interest in SEC careers.

To enhance our hiring capacity, we have requested 33 additional positions for the Office of Human Resources to help recruit and sustain the new personnel requested for FY 2014. These expanded capabilities will allow the agency to effectively implement the planned workforce expansion envisioned in the FY 2014 request.

### *Information Technology*

**Question: The fiscal year 2014 budget request includes \$56 million for information technology investments, in addition to the \$50 million Reserve Fund, which will be used for large, multi-year IT projects.**

**How will an increase in information technology help the SEC perform oversight of increasingly complex markets?**

**Response:** Information technology enables the SEC to work smarter through increased productivity, improved decision-making, and more efficient business processes. It allows us to access information with speed and accuracy, conduct predictive analysis, study trends, and spot anomalies.

Key to the SEC's effectiveness is our ability to research and mine large volumes of data in order to locate and act upon the proverbial "needle in the haystack" that may provide evidence of wrongdoing. Data often holds the answers, but it also presents one of our biggest challenges: with the increasing size and complexity of the markets, the amount of data grows with each passing second. Analyzing this data presents significant challenges, and we currently lack the mechanisms to thoroughly and effectively search and identify correlations within or between large data sets.

A key first step in addressing these challenges is the Enterprise Data Warehouse ("EDW"), which will enhance data quality and consistency, save time by allowing users to quickly search and access critical data from one place, and provide historical intelligence by allowing users to analyze different time periods and performance trends in order to make future predictions. Data integration and enhanced analytical tools will allow seamless searches of data sets to examine activity to reveal suspicious behavior quickly trace the origin. The SEC is currently in year one of a multi-year effort to consolidate the numerous data sources both inside and outside the SEC onto this EDW platform.

Another key information technology investment that the SEC is making to support its core mission is in the EDGAR Modernization program. The EDGAR filer system allows companies and individuals to file periodic reports and information to the SEC and allows SEC staff and the public to search the filings. The EDGAR filer system was developed

in the mid-1990s and was partially modernized in 2001. The system has numerous issues such as multiple filing formats, complex file numbers, hard coded OMB dates, cumbersome hard copy fee processing punch lists, and structured data problems. There is significant need to incorporate business processes that do not exist within the current system, such as: mergers and acquisitions, enforcing entity data upkeep, and a structured data format that will facilitate movement and storage of EDGAR data in the EDW to facilitate analysis of the data across the SEC. EDGAR Modernization will improve the SEC's ability to meet Commission requirements in a more timely manner and ultimately will reduce the annual operations and maintenance costs for the system.

**The testimony mentions that one of these IT improvements, the Enterprise Data Warehouse, is going to enable the agency to combine different sources of data to enhance analysis. In other words, you will be able to “see” across different databases with ease, which will help you catch problems much faster. This is a big step for the SEC.**

**Question: When do you anticipate this system will be up and running?**

**Response:** The Enterprise Data Warehouse (EDW) is currently in the first year of a multi-year effort to enable the SEC to combine data from different sources to enhance analysis and decision making. This multi-year plan is comprised of components and efforts that are already up and running, projects that will be implemented in the near-term, and longer-term initiatives that will kick off later this year and span the coming months and years. We estimate that the EDW will be fully deployed from a development perspective in FY2015, with expansion in future years as capacity and new requirements are defined.

Below is a brief overview of the EDW Plan:

- **Up and Running** - EDW Infrastructure (hardware, software and connectivity) has been procured, installed, and tested and is currently targeting “approval to operate” in the next several weeks. At that point, projects will have formal approval to leverage the new data warehouse environment.
- **Near-term** – SEC staff is actively engaged in requirements analysis for several pilot projects across divisions. The goal of these projects is to demonstrate incremental value to the agency while applying a “test and learn” implementation approach to ensure well-managed delivery. It is anticipated that following detailed project planning the first of these pilots would be implemented during the 2013 calendar year.
- **Long-term** - A Blanket Purchase Agreement (BPA) has been developed for larger scope work efforts, the first of which will include EDGAR Data Provisioning and Financial Data Mart efforts. This solicitation is on-track for release in the near future and a third quarter award.



- **Ongoing** - Planning and work around standards, practices, organization and governance required to support the EDW is well under way to support current pilot capability delivery efforts.

As divisional data is loaded to the EDW in the coming months and years, both the SEC and public will benefit from the enhanced decision making, more timely analysis, improved data quality, and consistency that a consolidated EDW will provide.

### *Enforcement Priorities*

**I was concerned to read we will soon hit the statute of limitations on misconduct during the 2008 financial crisis. Although there have been several enforcement actions against a number of entities responsible for causing the crisis, it seems as though we may let a number of individuals, banks, and others slip through the cracks.**

**Question: What are your thoughts on areas where SEC enforcement can be more vigorous?**

**Response:** As described below, the SEC's pursuit of financial crisis-related actions has been extremely effective, as have the efforts to crack down on insider trading by major Wall Street and other financial industry professionals. Similarly, pursuing misconduct by investment advisers and broker-dealers has been a key focus of the SEC's enforcement program in recent years.

Beyond those efforts, I have encouraged the Enforcement Division to continue to prioritize its focus on market structure issues, a capability that has been enhanced by the work of the Division's Market Abuse Unit. The issues include ensuring that fast-moving technology does not confer an impermissibly disparate informational advantage to certain market participants, and could touch on areas such as high frequency trading, complex trading algorithms, dark pools, and intricate new order types. In furtherance of this enforcement objective, to ensure fair trading and equal access to information in the securities markets, the SEC brought several significant actions in the past year against stock exchanges, alternative trading platforms, broker-dealers, and other market participants. Noteworthy cases included actions charging:

- the New York Stock Exchange with providing certain customers with favored access to data that could be used to make investment decisions;
- dark pool operator eBX LLC with failing to protect the confidential trading information of its customers;
- brokerage firm Hold Brothers On-Line Investment Services with allowing foreign traders to access the markets and conduct manipulative trading through an illegal practice known as "layering;" and

- Pipeline Trading Systems LLC and two of its top executives with failing to disclose to its customers that most orders placed on the dark pool trading platform were filled by a trading operation affiliated with Pipeline.

In addition, I am focused on ensuring that Enforcement devotes sufficient resources and attention to the areas such as accounting fraud, including issuer reporting violations and auditor misconduct, as well as on those frauds that have an impact on particularly vulnerable retail investors.

Further,

As our fiscal year 2014 budget request recognizes, the SEC must expand its enforcement function to keep pace with the growing size and complexity of our markets and the SEC's additional responsibilities, and to send strong messages to wrongdoers that misconduct will be swiftly and aggressively addressed. Additional resources are needed in Enforcement to further refine our analysis of incoming tips and leverage incoming data to identify trends of possible misconduct across product, sectors, or geographic areas. We also need to engage additional industry experts and proactive data analytics to better target industry practices that may harm investors. For example, we have developed certain algorithms to mine publicly available hedge fund performance data to identify aberrational performance returns that could be indicative of conduct warranting further investigation. With additional front line investigative attorney, trial attorney, and forensic accountant resources, we would further bolster our core work of pursuing potential securities laws violations identified from these and other sources. The Division of Enforcement would focus its hiring of 131 requested staff on increased expertise in the securities industry and new product areas, trial attorneys, and forensic accountants, as well as staff for the division's Office of Market Intelligence, the Office of the Whistleblower, and the SEC's collections and distributions functions.

**Question: Do you think there is more to be done to ensure accountability for our 2008 financial meltdown?**

**Response:** The SEC has a strong record of cases holding accountable those institutions and individuals who engaged in misconduct related to the financial crisis. To date, the SEC has filed crisis-related actions against 157 entities and individuals, including more than 65 CEOs, CFOs, and other senior corporate officers at some of Wall Street's most sophisticated banks and institutions, including Goldman Sachs, J.P. Morgan, Citigroup, Wachovia, Wells Fargo, Bank of America, Bear Stearns, Fannie Mae, Freddie Mac, Countrywide, New Century Mortgage, and other large financial firms. These actions have resulted in \$2.68 billion in total penalties, disgorgement and other monetary relief for investors, as well as industry bars for wrongdoers.

While these results are very impressive, the metrics alone do not adequately capture the complexity and sophistication of the transactions and products involved in the agency's financial crisis-related cases. Our ability to harness the expertise of our enforcement

staff, including through recently-created specialized units and the deep experience of industry experts, has been and will continue to be critical to our success in this area.

We have pursued our financial crisis-related investigations with vigor and, while we expect the remaining cases arising from the financial crisis to be brought or resolved in the near future, as in all of our investigations, we remain focused on achieving true accountability for those whose conduct harms U.S. investors.



TUESDAY, MARCH 19, 2013.

**GENERAL SERVICES ADMINISTRATION**

**WITNESS**

**DANIEL M. TANGHERLINI, ACTING ADMINISTRATOR, GENERAL SERVICES ADMINISTRATION**

Mr. CRENSHAW. Good morning, everyone. The hearing will come to order. Welcome to the Subcommittee members and to our witness, Acting Administrator Dan Tangherlini of the General Services Administration. Welcome to all of you and thank you for your public service, and that of your staff. Last year, as you know, GSA made headlines, but for all the wrong reasons. Lavish spending on conferences, food, and entertainment; employees accepting gifts from inappropriate sources; excessive spending on relocation expenses, travel for virtual employees, and employee award programs; and most troubling, non-compliance with federal procurement law. Now, GSA is supposed to be the federal government's procurement expert, but disregard for procurement laws, regulations, and policies is what got GSA into trouble. I am committed to preventing this kind of outrageous behavior from taking root again at GSA, and I know that you all are, too.

So you are here today because you are committed to expelling waste and extravagance from the GSA, and making GSA more efficient and more accountable. This Committee appreciates your commitment, but I believe Congress needs to continue to closely oversee your activities to ensure that the funds entrusted to the GSA are spent appropriately. In order for our bill to move through the appropriations progress, we will need to convince our colleagues on both sides of the aisle that GSA has changed. And for years, this Subcommittee has been pushing GSA to make better use of its existing portfolio of buildings. And to that end, we included a square foot limitation on GSA's inventory of leased and owned space in our 2013 House bill. And I was heartened to learn that the administration is now working on how to implement that freeze through the federal government's real estate footprint. The next step is to reduce the footprint.

Staffing levels at the federal agencies are falling, and, with that, so are their office space requirements. In combination with disposing of surplus properties, a reduction in GSA's real estate portfolio is within reach. We are not here to discuss the 2014 budget because we do not have it yet, you do not have it yet, and we hope to have it soon. But I am hopeful that initiatives like the freezing of the footprint are incorporated into the President's budget. And that way, we can begin to reduce the Federal Buildings Fund's expenses. I hope together with our staff that we can work closely to unlock the potential for hundreds of millions of dollars of savings

each year, through improved property management and procurement. If we can, then we can restore the American public's trust in your agency.

Once again, welcome. I appreciate your service and I look forward to hearing your testimony. Now I would like to turn to my friend and colleague, Ranking Member Serrano, for any remarks he might have.

Mr. SERRANO. Thank you, Mr. Chairman. I would like to join you in welcoming acting GSA administrator, Dan Tangherlini, before the Subcommittee. The General Services Administration plays an important role in the federal government, both as a landlord and as a procurement hub. I will be interested in hearing how the sequester and the related budget uncertainty are affecting you, both directly and indirectly, through your role as a supplier for other agencies. With this central role as a supplier, the GSA has an opportunity to do a lot of good for the federal government by improving efficiency and helping agencies to bring down their cost. Unfortunately, the agency's mission has been obscured over the past year by various controversies. Entering in their wake, you obviously faced a large challenge. I look forward to hearing how things are going at the agency now that you have had some time to get your feet under you and understand what the agency needs to improve.

I know that on the property management side you are currently dealing with costs related to excess rental properties. Although you must deal with the impact of the sequester, I am interested in learning what steps you are taking to consolidate agencies into federally-owned space. With a still recovering economy, it would seem like a good time to invest in new buildings that would save us money in the long run.

The GSA plays a major role in ensuring that our government is operating efficiently. That role is even more important as sequestration continues. I am concerned about whether, with the sequester, you have sufficient resources to do that job. I look forward to your testimony on this and other issues, and I thank you for appearing before us today.

Thank you, Mr. Chairman.

Mr. CRENSHAW. Thank you, Mr. Serrano. I would like to now recognize Acting Administrator Tangherlini. If you could keep your remarks to about five minutes or less, we will have more time for questions, and your written statement will be made a part of the record. Please.

Mr. TANGHERLINI. Yes, sir. Thank you very much, and good morning, Chairman Crenshaw and Ranking Member Serrano, and members of the Committee. Thank you for allowing me to appear before you today. And at a time when budgets are tightening across the government, the work of GSA is more important than ever before.

I was appointed by President Obama almost a year ago as the Acting Administrator of GSA, in the wake of some very well-publicized mistakes at the agency. For my first day on the job, I worked with the women and men of GSA to ensure that such a breach of trust would never happen again. One of my first tasks was to start a top-to-bottom review of the entire agency that examined every aspect of how GSA operates and what reforms could be

implemented to help us better accomplish our mission. This review gathered comprehensive feedback from employees at every level of GSA, as well as the businesses and federal agencies who work with us.

As a result of what we have learned, I have implemented a number of common sense reforms to save taxpayer dollars, increase accountability, and make GSA a more efficient organization. This past fiscal year, we reduced our spending on travel, IT devices, and printing, to end the year 43 percent lower than our fiscal year 2010 baseline for those items. In travel alone, we saved \$28 million by revising our internal travel and conference policies. Last year, we reduced bonuses throughout GSA by 64 percent.

In addition to all this, we created more than \$5 million in savings directly from employee suggestions through something we call "The Great Ideas Hunt." These are significant savings. But if we are going to provide our partner agencies with the services they need, it is important that we ensure our own agency is operating as efficiently and effectively as possible. The top-to-bottom review has shown a widespread duplication of support services throughout the agency. In response, we are consolidating several of those administrative functions to strengthen and support GSA. Consolidating administrative activities enables us to align and streamline the way we provide services, such as IT, HR, and Finance. This will increase transparency and accountability throughout the agency. It will also improve the quality of these services for our own employees. If we can provide the most effective and efficient services possible in our own operation, then we will be able to fulfill our mission of delivering the best value in real estate, acquisition, and technology services to the government and the American people. I thank the Committee for their cooperation and suggestions in development of this consolidation effort.

Our job is to get the most out of every dollar so that our federal partners can focus on their own missions. GSA has the expertise and the ability to deliver significant savings for our partner agencies. Through the buying power of the federal government, we are able to negotiate leases that, on average, are more than 11 percent below market rates. This has created an annual savings of \$30 million across our lease portfolio in realized cost avoidance. We also work aggressively to ensure that the facilities we own are being used to the maximum extent. Nationally, GSA's vacancy rate is 3.1 percent, far below the private sector average of 17.4 percent. In fact, if our vacancy rate was as high as the average in the private sector, it would cost the taxpayers an additional \$1 billion in this year alone.

In addition to helping customer agencies save on space, GSA's strategic sourcing initiatives create significant savings by getting agencies to collectively commit to purchasing certain commodities at the best value. By buying once and buying well, strategic sourcing has saved the American public more than \$300 million since 2010. GSA has also been able to negotiate prices for our office supplies that are 13 percent below what we have previously paid. This has already saved more than \$127 million. At the same time, we realized these significant savings; we also need to ensure that we directed expenditure towards small businesses. Seventy-six per-

cent of the dollars spent in that office supplies strategic source initiative went to small businesses.

GSA is committed to the continued evaluation of our own processes so that we can find innovative ways to provide greater value to the American people. But our work is far from done and I am confident that, with your support, we will continue to find common sense reforms within GSA.

I thank the Committee for the opportunity to testify today and I look forward to answering your questions.

[The information follows]



**STATEMENT OF DANIEL M. TANGHERLINI**  
**ACTING ADMINISTRATOR, GENERAL SERVICES ADMINISTRATION**  
**BEFORE THE HOUSE APPROPRIATIONS COMMITTEE**  
**SUBCOMMITTEE ON FINANCIAL SERVICES AND GENERAL GOVERNMENT**  
**MARCH 19, 2013**

Chairman Crenshaw, Ranking Member Serrano and Members of the Subcommittee: My name is Dan Tangherlini and I am the Acting Administrator of the General Services Administration (GSA). Thank you for inviting me to appear before you today.

The scope and breadth of GSA responsibilities are both wide-ranging and essential to the federal government. With over 12,500 employees across 11 regions, the mission of GSA is to deliver the best value in real estate, acquisition, and technology services to the government and the American people.

As the landlord and caretaker for federal properties, GSA owns or leases 9,624 assets, maintains an inventory of more than 370 million rentable square feet of workspace, and preserves more than 481 historic properties.

GSA has an annual business volume of over \$60 billion, manages over 200,000 fleet vehicles, assists tens of thousands federal travelers through GSA's electronic travel system, and serves as the focal point for data, information and services offered by the federal government to its citizens.

***Reforming GSA***

GSA has made some well-publicized mistakes and we have revised our internal policies and increased oversight to ensure that they do not happen again. I initiated an agency-wide Top to Bottom review to examine every aspect of GSA's internal operations and spending practices, and assessed the agency's effectiveness in fulfilling its mission. During this process we held dozens of meetings with employees and senior agency officials to examine the underlying root causes that led to the 2010 Western Regions Conference. We conducted in-depth interviews with our customer agencies to assess the quality of our service delivery and listen to their needs. We also spoke with leading executives in real estate, procurement and government transformation, such as Blackstone, Deloitte, and Hewlett-Packard, to identify common-sense best practices from the private sector that can help improve GSA's operations.

As a result, we have implemented a number of reforms to prevent the waste of taxpayer dollars, increase accountability and make GSA a more efficient organization. We have reduced spending on printing, travel and IT devices and ended FY 2012 43 percent below the 2010 baseline for printing, travel, and IT devices. In travel alone, we saved \$28 million dollars by

revising our internal travel and conference policies. Last fiscal year we reduced bonuses by 64 percent. I asked GSA employees for suggestions on how we can be more efficient in the "Great Ideas Hunt." Their ideas will generate another \$5 million in savings.

### ***Clearing up our structure to improve oversight and accountability***

The Top to Bottom review also revealed larger structural problems within the organization. The decentralized structure of GSA created a lack of coordination, duplicative investments and variable performance. To address these issues, we are consolidating key support functions to eliminate redundancies, increase agency efficiencies and allow our major business units to focus on core missions.

The consolidation process began last April, when I directed the PBS Chief Financial Officer to report to GSA's Chief Financial Officer. We are also bringing all information technology personnel, budgets, and systems under the authority of the Chief Information Officer. The result will be a technology office that has the ability to directly provide all IT services across the entire agency and ensure that future technology investments are reviewed on an enterprise-wide basis.

Other functions undergoing consolidation include human resources, administrative services, emergency response, small business outreach, and congressional affairs. The efficiencies generated through these consolidations will free up resources we can invest in improved delivery of our core mission-focused services.

### ***Helping agencies focus on the core mission***

With budgets tightening across the federal government, GSA is in a unique position to help agencies save money on a wide range of support activities so they can focus on their core mission.

#### ***1) Real Estate Expertise***

GSA has expertise to help agencies in every stage of the real estate process: acquisition, operations, and disposal.

Through economies of scale, GSA is able to negotiate rates in our leases below market. For example, in FY 2012, when we measured GSA leases against the market we were, on average, 11.5 percent below market rates. This resulted in a cost avoidance of \$30 million for customer agencies, realized annually.

GSA also helps agencies operate space more efficiently, reducing energy usage and utility costs. GSA's Public Utilities program provides contracting vehicles that enable agencies to procure utility services at the lowest cost and the greatest value to the government. Our services cover the procurement of electricity, natural gas, water, and sewage services.

For agencies in GSA-owned space, we have also realized savings by installing Advanced Metering systems in federal buildings. For example, in the New England region, 26 buildings have systems monitoring electricity and water consumption, 11 buildings monitor natural gas, 5

monitor steam and 3 monitor oil. As a result, GSA buildings in the New England region will save \$316,000 annually through reduced energy usage.

GSA works aggressively to maximize the utilization of our existing inventory. Nationally, GSA's vacancy rate is 3.1 percent, far below the private sector average of 17.4 percent. If our vacancy rate was as high as the private sector, it would cost the taxpayers an additional \$1 billion this year. GSA also works with agencies and the Office of Management and Budget to dispose of unneeded property. In FY 2012, GSA completed 126 disposal actions: 114 for customer agencies and 12 for properties in the PBS inventory. Proceeds from the sale of GSA properties totaled \$12.7 million.

Additionally, through public private partnerships, GSA is seeking to leverage the expertise of the real estate industry to solicit ideas on how to make more efficient use of the government's assets while also disposing of excess properties. Two such projects are the potential for a new FBI Headquarters and the redevelopment of the Federal Triangle South area of Washington DC.

Further, GSA has positioned itself to be a real estate asset manager for customer agencies. In 2010, GSA initiated the Client Portfolio Planning (CPP) program as a means to proactively assist federal agency clients with analyzing and optimizing their existing portfolios, while systematically anticipating, capturing, and advising on future requirements. This CPP program develops for customer agencies near- and long-term strategies to achieve optimal portfolio performance.

GSA continues to work hand-in-hand with the Administration in the implementation of Administration initiatives such as the "Freeze the Footprint" policy. To ensure full implementation of the "Freeze the Footprint" policy GSA will consult with agencies on how they can use technology and space management to consolidate locations, increasing occupancy rates in facilities, with the goal of eliminating lease arrangements that are not cost or space effective.

## ***2) Leveraging the Government's buying power through Strategic Sourcing***

In addition to helping customer agencies save on space, GSA's strategic sourcing initiatives save agencies money by leveraging the buying power of the federal government. Strategic sourcing initiatives identify the top value vendors for common goods and services and provide improved management of agency purchases.

GSA is working with the Office of Management and Budget (OMB) and partner agencies to create 10 new government-wide strategic sourcing solutions over the next two years which will cover a range of commonly purchased products and services – such as cleaning products, tools, and wireless devices. These initiatives will be in addition to those already in place for office supplies, domestic package delivery, telecommunications expense management services, and print management. Strategic sourcing initiatives have already saved the government over \$300 million.

## ***3) Reducing agency fleet and travel costs***

GSA provides a variety of tools and services to help agencies right-size fleets, improve fuel efficiency and reduce acquisition and maintenance costs.

GSA fleet leased vehicles are the least costly source of motor vehicles for the Federal government. By leasing through GSA, agencies save an average of nearly \$2,000 per vehicle per year. When agencies purchase a vehicle, GSA provides an average savings of 17.6 percent below manufacturer invoice.

In air travel, GSA's Airline City Pair Program (CPP) is estimated to save the Federal government \$5.9 billion on airline tickets compared to comparable commercial fares in fiscal year 2013. On lodging, GSA's FedRooms program provides federal travelers hotel rooms in over 13,000 locations at or below per diem rates. GSA's E-gov Travel Service (ETS) provides a comprehensive end-to-end solution for travel management and is estimated to save agencies \$16 million per year. Finally, GSA has established the Government-wide Travel Advisory Group (GTAC), comprised of industry and government travel experts, to examine government-wide travel regulations and issue recommendations on how to increase travel efficiency and effectiveness, reduce costs, promote sustainability, and incorporate industry best practices.

#### ***4) Enhancing Government-Citizen Engagement***

GSA also contributes to a more open, transparent and secure government by developing innovative solutions for federal agencies to save money and enhance citizen engagement.

The Federal Risk and Authorization Management Program (FedRAMP) provides a standardized approach to security assessment, authorization, and continuous monitoring for cloud products and services. GSA was the first government agency to move to cloud computing in June 2011, saving \$4 million dollars to date and setting an example for others to follow.

Data.gov has developed 7 new communities than span multiple agencies data catalogs, and provided data services on to users in a way that provides a costs avoidance for agencies of \$14.3 million.

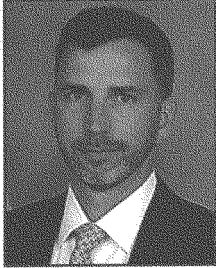
#### ***Conclusion***

In a time of increasing budgetary constraints, GSA's products and services help agencies save money, become more efficient, and focus on the core mission.

We know that every taxpayer dollar counts and we are committed to using it as efficiently as possible. We will continue to examine our processes and look for more innovative ways to provide greater value to the American people.

Our work is far from done. Your support is an essential step for continuing positive change and common sense reforms within GSA. I thank the committee for the opportunity to testify today and look forward to answering your questions.

## Dan M. Tangherlini - Acting Administrator



Dan M. Tangherlini was appointed acting Administrator of the U.S. General Services Administration (GSA) on April 3, 2012, and serves a vital role in President Barack Obama's agenda to build a more sustainable, responsible and effective government for the American people. GSA is responsible for improving the government's workplace by managing assets, delivering maximum value in acquisitions, preserving historic property, and implementing technology solutions.

Throughout his career, Mr. Tangherlini has been recognized for fiscal and management leadership. Before joining GSA, Tangherlini was confirmed by the United States Senate in 2009 to serve as Treasury's Assistant Secretary for Management, Chief Financial Officer, and Chief Performance Officer. In these roles, Tangherlini served as the principal policy advisor on the development and execution of the budget and performance plans for Treasury and the internal management of the Treasury and its bureaus. Tangherlini also served as the agency's Director of the Office of Small and Disadvantaged Business Utilization.

From 2006 to 2009, Tangherlini also served as Washington, DC's City Administrator and Deputy Mayor. His responsibilities included managing the day-to-day operations, budget development and performance management of District agencies. Tangherlini also served as the Director of the District of Columbia Department of Transportation (DDOT) from June 2000 to February 2006.

Prior to his appointment as City Administrator, Tangherlini served as the Interim General Manager of the Washington Metropolitan Area Transit Authority. Tangherlini also served the District of Columbia as Chief Financial Officer of the Metropolitan Police Department from November 1998 to May 2000. Before joining the District government, Tangherlini worked in the Policy Office of the U.S. Secretary of Transportation and in a variety of capacities during six years of service with the Office of Management and Budget in the Executive Office of the President.

Tangherlini received his Bachelor's and Master's degrees in Public Policy Studies from the University of Chicago and his Master's degree in Business Administration from The Wharton School of the University of Pennsylvania.

## SEQUESTRATION

Mr. CRENSHAW. Well, thank you very much. Let me start the questions by picking up on what Mr. Serrano said in his opening statement, this whole issue of sequestration. You know, you are not really impacted, other than a few small policy offices. You are not really impacted in the sense that your clients pay you, they have experienced a cut, and if we cut you, then that would be a double cut. So you are in a sequester-free zone. And it almost makes your obligation even stronger to make sure that, as you work with people that are experiencing these cuts, to be as efficient as you can. And I just wonder, you know, we all agree here that we would rather be able to have targeted cuts and say this is something working, and we, maybe, add additional revenue; and here is a program that is not working and we might eliminate it. But we are living with a sequester.

And I wonder, from your standpoint, as you deal with these agencies that are going through these cuts, what are they saying to you? Are they kind of clamoring to have lower rents, or whatever you are providing for them? And can you give us an idea they are being impacted as it relates to what you do? And then also, do you help them in ways that they might, when they look at these cuts, and they have to be more efficient, and they have to find places where they can spend less, are there ideas that you have in your exchanges with them? Could you touch on those two things?

Mr. TANGHERLINI. I think that is a fantastic question, and I appreciate the thoughtful approach to it because, yes, GSA does not have much in the way of direct impact on the organization because so little of our resources are directly appropriated. Most of our funds come through rental payments to the Federal Buildings Fund or through industrial funding formula money that comes out of people making expenditures through the Federal Acquisition Service into the Acquisition Services Fund; if you think about it, since we are downstream from those cuts, that has a long-term impact, one that we are very concerned about, and looking at it, very closely, for the organization. More importantly though, to your point, really, it challenges us to recognize that our role, the whole reason why we were set up as an organization, was frankly to leverage the scale of the federal government; to drive down the costs of basic, common administrative services and operations.

And so shortly after I got over to GSA, I started visiting my colleagues over at other agencies, meeting with deputy secretaries and secretaries, and saying, "What could we do to help you save money?" And I was always cordially received, but I have to say, I am pretty enthusiastically received right now. And we are trying to find specific actionable projects around rent consolidation, around common acquisition; the strategic sourcing initiative that has been led by OMB, in particular, has received an awful lot of interagency support.

So I think, really, this is the time for GSA to show its value. This is the time for GSA to demonstrate its worth and to really make amends for things that happened leading up to my being here. I think this is really an important time for GSA to show what we can provide agencies in the way of savings and solutions.

Mr. CRENSHAW. Thank you very much. Mr. Serrano.

#### TOP-TO-BOTTOM REVIEW

Mr. SERRANO. Thank you, Mr. Chairman. Mr. Administrator, you have been at GSA for almost a year now and you have undertaken a complete examination of the agency in that time. I appreciate the opportunity to ask you about the top-to-bottom review that you instituted at GSA, and I want to start just generally. What has been the biggest surprise to you in getting to know this agency?

Mr. TANGHERLINI. Well, I have to say the biggest surprise has been a pleasant surprise. And that is how many high-quality, committed, dedicated public servants there are at the organization. What I found is that some of the folks who are most enraged and upset about, you know, the events of last Spring, the revelations of last Spring, were the people who worked at GSA who had committed decades of their lives; they committed their public service careers to making this organization better, every day. I also found, though, that there are opportunities where GSA could take a little bit of its own medicine; where we could cooperate and collaborate more; where we could share and rely on each other more; where we could leverage our own scale as an organization; where we could do things once and well within GSA, and get a better, more efficient GSA. That is what led us to bring before this Committee a description of what we are calling CXO, and that means CIO, CFO, Chief People Officer, consolidation activities, so that we could get much more efficient as an organization and do a better job of serving our agency partners. But we have just started down that road. I think that the key outcome of the top-to-bottom review is that any good organization never stops reviewing itself from top to bottom.

Mr. SERRANO. And speaking of organizations, you have had experience with many different agencies. What did you find at GSA, when you did find deficiencies? Are these unique to GSA? Have you seen them elsewhere? And, in asking that, how is GSA different than other agencies you have dealt with?

Mr. TANGHERLINI. Well, I have never worked at anything quite like GSA. You know, the mandate that GSA has is so substantial, and the size of the impact the organization has on the government is bigger than anything I have specifically led before. But there are a lot of common problems across these organizations. Having transparency and visibility into good information so that you can make solid managerial decisions is a deficiency I have found in many of the jobs that I have worked on.

What I can say is unique and special about GSA is the role we play in supporting every other agency's mission. And it is a very important role; it is easy to forget, it is kind of like the plumbing in a house. It is not the kind of thing you think about until it is broken. And no one gets excited about it when it is broken; no one is happy to pay to plumber's bill. So we have to figure out a way that we can more effectively, and efficiently, and reliably provide those services; provide good, solid information to decision makers such as yourselves; give good feedback within the organization to our agency partners. And I think, in general, just do a better job

of trying to be more transparent and more clear about places where we can make continuous improvement.

Mr. SERRANO. You know, when those issues came up regarding travel, and conferences, and so on, it opened up the door for some folks, some of my colleagues, who are not crazy about GSA to begin with. And you cannot blame them, in a way. It was a pretty bad situation. So there has been so much criticism of GSA. Now I want to ask you a different question: What can we be doing to help you? Besides giving you more dollars, which is always a difficult thing around here these days. But what can we be doing to help you as you undertake not only the full study, but you are charged with the responsibility now of turning this agency around from the perception that it was failing in so many ways.

Mr. TANGHERLINI. I really appreciate your asking that question, because I think we need a collaborative partnership focused on the same outcomes, and I frankly think a well-running GSA is not a partisan issue. This is the basic operations of government. This is the basic underlying administrative services that support these vital missions of working to cure cancer, and protecting our border, and supporting air traffic control; those core basic things that the government does.

So I think engaging in an ongoing dialogue, understanding what our limitations are, understanding, perhaps, some of the complexities that we face; working to recognize the value of high-quality, efficient service delivery on the facilities side, as well as on the acquisition services side; helping us make the appropriate information technology investments so that we can support agencies in operating more efficiently; giving them more transparency into their spending so that they can operate more efficiently; I think that is the kind of partnership that we could continually work on developing.

Mr. SERRANO. So, Chairman, before I yield my time, just something that you have been a part of and other members of the Committee, this Subcommittee, more than any other place in Congress, has been very active in reminding all federal agencies that besides the 50 states, we have territories. And I personally take a big interest in that, as you'll see me tonight rooting for one of the territories in the World Baseball Classic. But we hope that sometime down the line you can tell us, without, you know, bogging you down with a report, on what is the work the GSA does in the territories, how it responds, and, in general, to remember that while they may not be states, they are still American citizens and should be treated equally.

Mr. TANGHERLINI. I appreciate that. As you can see from my bio, I was the city administrator and deputy mayor here in Washington, District of Columbia; not exactly a territory.

Mr. SERRANO. Close.

Mr. TANGHERLINI. But in that experience, gained some sensitivity to the unique nature of the "non-state" parts of the United States.

Mr. SERRANO. Thank you so much. Thank you, Mr. Chairman.

Mr. CRENSHAW. Thank you, Mr. Serrano. Mr. Bonner.



## FEDERAL COURTHOUSES

Mr. BONNER. Thank you, Mr. Chairman. I am going to admit upfront I am going to be parochial with my questions, and I told the Acting Administrator upfront of my concern. We have been trying to get a new federal courthouse in Mobile, Alabama for 18 years. And 18 years ago, I had a lot more hair than I have got. I was in my 30s and not my 50s. And with the pressure on the budgets and the pressure on all agencies to cut back, I told the Acting Administrator in private, if we are going to have a total freeze, we are not going to have any construction, or any renovations, or any new starts anywhere in the country or its territories.

I would never ask that you put a project in my district on the starting block. That would be hypocritical of me. But once we started and got down the path on this journey, 10 years ago, GSA actually came up with the recommendation that we needed a new courthouse. We needed it because the old courthouse has a leaky roof; well, you can repair that. We have got mold and mildew, and it has got a lot of problems, as GSA has noted.

Under the leadership of the chairman at the time, Mr. Serrano, we elevated the concerns to the point that when we got to the starting point, when we made it on the GSA list, not our list, but the GSA list to be eligible, we would be teed up and ready to go. Had this thing called a stimulus bill back in 2009; they were looking for shovel-ready projects. This was a shovel-ready project. And, again, thanks to the leadership of the former chairman, current ranking member, we were able to put a downpayment on some \$50 million into the funding of this. Fast forward, here we are in Mobile, as I understand, it is currently number one in line. Now, again, if we are not going to do any construction anywhere in the country, then I can certainly accept that.

So my question to you, Mr. Tangherlini, is, is Mobile still in the number one spot in terms of federal courthouses that are on the list to be constructed?

Mr. TANGHERLINI. The simple answer is that from the list prepared by the Administrative Office of the Courts, the Mobile courthouse is still the number one courthouse for a replacement investment.

Mr. BONNER. Okay. With that response, recent developments lead me to be concerned that there may be an effort to reconsider this. A review was ordered. The initial feasibility study was, as I understand it, shelved; a new feasibility study has been ordered. So my question is two-pronged on that. To your knowledge, and if you cannot answer this today, if you could look into it and respond back to us, are the judges in Mobile being involved at every step in terms of this new feasibility study? And is their input being sought in terms of, if we are downsizing space of the building, you would think you would be able to get the building closer to the money we currently have or close to it. So are the local judges being involved in this new phase of this, and could you tell us where they are?

Mr. TANGHERLINI. No, I appreciate that. It is my understanding that the judges are involved in every phase, that we do involve the local judiciary in these discussions. There is a broader set of standards that Administrative Office of the Courts have developed. They

actually have developed now a five-year plan, which is, as you know, over the last 18 years, quite substantial progress in the way we manage, administer, rank, prioritize these courthouses. At the same time, through a lot of pressure, financial pressure on the organization, pressure from this body as well, Administrative Office of the Courts have been looking at how you shrink the space needs. Ideas like courtroom sharing have come into the fore since you probably started this journey. So I know there are ongoing discussions about that, trying to figure out how to move this project forward, understand what the resource needs are, but do it in a way that reflects the needs and the interests of the local judiciary. It is a lot to weigh in balance there.

Mr. BONNER. Well, courtroom sharing is one thing. Sharing an elevator for the judges and the people who have been accused of serious crimes is, from a safety standpoint, this building is so obsolete. So can you tell us, and Mr. Chairman, I am going to submit most of these questions to the record. But I would like to know, from your perspective, Mr. Tangherlini, how will OMB's "Freeze the Footprint" initiative impact the current status, the feasibility study and the status of the Mobile courthouse, if any?

Mr. TANGHERLINI. It is a great question. I am afraid I do not have a clear answer for you. But I can talk a little bit about the Freeze the Footprint program in general. The idea is to look across agency assets and try to freeze, and frankly, also decrease the square footage across agencies; in this case, we would look at the entirety of the judiciary. And so at the same time we are asking questions about the investment; in Mobile, for instance, we are looking at, say, the replacement of the L.A. courthouse which will shrink from 800,000 square feet to 500,000 square feet. So net-net, we are going to try to arrive at a freeze, and, frankly, our own goal is to try to also find ways to help agencies drive it down, because every dollar spent on space is one dollar less spent on program or return to the taxpayers.

Mr. BONNER. I would say that, as I understand it, I might be mistaken, but as part of the review of the need in Mobile, one of the factors was that the Marshal Service was going to need less space, the U.S. Attorney's office moved out, they moved to a commercial space because the current building was not adequate for them. I do not know whether we know with certainty whether they would consider moving back in the new building once it is constructed if that were an option for them. I know I am in a commercial building because, again, there was not space in the federal building in Mobile. So, again, Mr. Chairman, I apologize to take up time with the Committee on something that is important to me, but I guess the final point I want to make is, is that, in a bipartisan way, Chairman Serrano, Chairwoman Emerson, now Chairman Crenshaw, we have limited ourselves in terms of our ability to have input in some of the decisions that the executive branch makes. That is a discussion for another day. But I think when a building makes it up to the top of the list, and there has been previous expression of intent by Congress to support the list, and not politicize it, but to support it, I just hope that we can make sure that those opportunities continue to go down that path. Thank you, Mr. Chairman.

Mr. CRENSHAW. Thank you, Mr. Bonner. Mr. Serrano has a comment he would like to make.

Mr. SERRANO. Just to say for the record what the gentleman has said is totally correct. This has been, was, is, in my opinion, I hope, a top priority for this Subcommittee. And as ranking member, I still support the project that this Committee supported with great strength and with dollars at that time. And we do not know what has happened, but everything the gentleman has said is correct, and I just wanted the record to show that. Thank you, Mr. Chairman.

Mr. CRENSHAW. Thank you, and thank you, Mr. Bonner. Now I will turn to Mr. Yoder.

#### FEDERAL REAL PROPERTY PROFILE

Mr. YODER. Thank you, Mr. Chairman. Mr. Acting Director, thanks for coming today, and I appreciate your testimony. One of the things we are endeavoring to do is we look to try to balance the federal budget, get our books balanced here, find smart ways to reduce spending, and I think that is hopefully the goal of every member on this Committee, is to find ways to run all of our agencies and federal government the most efficiently and effectively to save tax dollars for the hard-working Americans that pay them.

And so I wanted to discuss a little bit about the property that the federal government owns, and specifically how we determine what property we own, where it is located, how the public has access to that. And I thought you might speak about that a little bit, and I had a few questions for you. First of all, is the GSA real property profile available to the American people? Is there a website, for example, we can go to and look for property the federal government owns? Does the GSA have the real property profile in a geographical information system, GIS? Is there a map I can click on, look for government land and buildings? So how is that information accessible to the public?

And then second of all, not only how we account for it, how it is accessible, but do we keep statistics on things that the federal government owns? Specifically, how many parking garages does the federal government own? How many golf courses does the federal government own? How many hotels does the federal government own? How many grocery stores does the federal government own? I think bringing that information to light would help the country have a dialogue about where we can reduce some of our property containment in a way that might save taxpayer dollars.

Mr. TANGHERLINI. Now I think your points are excellent, and I think that is key to managing the organization better. Any good business is always looking at what its assets are and how it can maximize the best outcomes of them. I think you have to understand, in a way, the relationship of GSA to federal property. We actually only own, or control, or manage about 10 percent of the entire federal government's federal property assets. We assist the OMB in developing the Federal Real Property Profile, but that data is entered entirely by other agencies, and so agencies have to maintain and update that data. We have made big strides in transparency in that data internally, just beginning the ability to share it among agencies and getting visibility into it within a GSA.

But to your point, I think there is still a lot of work that we can do. And I commit to working with this Committee and with other agencies in OMB to try to find ways to give people more understanding and better window into what the real property assets of the federal government are. I think it is for that reason why the Administration has put forward—and we have seen other proposals, both in the House and the Senate—for something along the lines of a civilian BRAC process by which you would really dive into the issue and ask ourselves: Where are those properties that are not getting the highest and best utilization? And how do we get them back into the economy? And, frankly, realize the results and the benefits.

Mr. YODER. Is there another agency that maintains the records of the real property that the federal government owns?

Mr. TANGHERLINI. So, each agency has their own real property management system.

Mr. YODER. But there's not one agency that would maintain all of the records on behalf of taxpayers and on behalf of the federal government.

Mr. TANGHERLINI. Not all of the records. What happens is each of the agencies need to upload information around a certain number of specific elements into something called the Federal Real Property Profile.

Mr. YODER. That occurs right now?

Mr. TANGHERLINI. That occurs right now. That system is maintained by GSA and overseen by a project run by OMB.

Mr. YODER. Okay, so GSA does have the information about every piece of property, and every building and entity that all the federal agencies own, because they are all required to upload that to you.

Mr. TANGHERLINI. We maintain the Federal Real Property Profile which has those elements, a certain number of elements, an agreed-on set of elements among the agencies, and then it is up to the agencies to ensure that they upload it.

Mr. YODER. So there is no policing to determine whether agencies are uploading it? Do we have an idea of how much compliance is being done? How much of the property that the federal government owns does GSA have logged into that database?

Mr. TANGHERLINI. Well, so, we only know what is logged into it, so we do not know what is not logged into it. And that is the problem. That is the delta you are looking for. The GAO has recently conducted a study that commented on the quality and the accuracy of the data. There are issues about the way we describe elements that could allow for the quality, the accuracy of the data to be degraded. So we are working very closely across the agencies to try to improve the quality as a demonstration of trying to get to the best possible quality. Within GSA, we did statistical sampling of properties within Region 4, the properties we controlled. And we found that we were within 97 percent accuracy.

Mr. YODER. But that is your own 10 percent that GSA owns.

Mr. TANGHERLINI. That is our own 10 percent.

Mr. YODER. So we really do not know how many properties the federal government owns. There is no one who can answer that question. GSA could not say that they had an accurate sample because they are dependent upon federal agencies to upload that in-

formation. I mean, so, I think you could say with some accuracy we do not actually have an understanding of the total amount of federal property that we own. We could not say with accuracy specifically how many parking garages we own, how many hotels we own, how many grocery stores we own. We just do not have that information.

Mr. TANGHERLINI. Well I think, I think the question is what level of accuracy.

Mr. YODER. Do we not have that information in an accurate format?

Mr. TANGHERLINI. Well, I think we have it in a format that has a level of accuracy. The question is, how accurate is it? And that varies agency by agency.

Mr. YODER. How accurate is it?

Mr. TANGHERLINI. Well, that, again, it varies agency by agency. I know that the GSA data is reasonably accurate as evidenced by our work done in Region 4. We are going to keep working on Region 4, and, in fact, we are going to work with a couple of other agencies to test their data as well. Some of it, as we have discovered, has to do with the way the elements are defined. An entire military base, this is a generalization, may be described as one asset. And you could have a facility on that asset that is of very low quality. You take a picture of that and you say, "Look, if the base is viewed as good, how can this thing with a roof caved in be considered good?" And so what we have to do is get a clearer statement of what those data element definitions are, make sure that the agencies adhere to those definitions, and then go back and check and police the data.

Mr. YODER. I just think you would agree, it seems like we cannot say with accuracy how many properties we own and we also do not know the level of accuracy of what we do own. So it is not that we know we are not completely accurate; we do not even know what level of accuracy we have. That is a real problem when it comes to managing the assets of the federal government and ensuring that we are properly spending resources. If you do not know what you have, how do you know how to effectively manage your resources and to make sure that taxpayers are not wasting dollars. I mean, the first step is knowing what we own, correct?

Mr. TANGHERLINI. And I think it is a concern we share. And that is why we have been so committed to working on these issues, that is why we have proposed the Freeze the Footprint. In order to freeze it, people have to have a better understand of how big the footprint is. That is why we have been committed to focusing on improving the quality FRPP data, as well as this idea of pushing forward ideas that we have seen. You know, proposals in both branches of Congress, both houses of Congress, that are based on the same theme of saying, "Look, we need to move forward on getting assets off the books that we do not need."

Mr. YODER. Certainly as we go forward in this process, efforts by the GSA that you are describing need to continue. I think we certainly need to improve those. And we need to work to fully understand where these assets are and to get our accuracy up to a level. I mean, 97 percent is GSA. We do not know what the accuracy is of the other agencies. And I think that is a real concern. And I

think the American people would love to be able to not only know what they own, but be able to go onto a database, and be able to go online and find it. And I think it would be astonishing to a lot of taxpayers that we do not have the ability to do that. And, Mr. Chairman, with that, I yield back.

Mr. CRENSHAW. Thank you. Mr. Quigley.

Mr. QUIGLEY. Thank you, Mr. Chairman. To my colleague's point, I think maybe Mr. Chaffetz had been speaking to him because Mr. Chaffetz and I have introduced legislation that would require the GSA to maintain a public database listing all federal properties, excluding certain properties in the Department of Defense for security reasons. But it raises an excellent point on all this. The bill also empowers the GSA to provide agencies with technical expertise to help them dispose of unneeded property, and creates a pilot program where GSA and OMB will identify and dispose of 15 high-value properties. So we are working along those lines, but certainly appreciate your support.

Mr. TANGHERLINI. In preparation for the hearing, I read your bill.

Mr. QUIGLEY. Now there is three that have.

Mr. TANGHERLINI. Yes, okay. I think there are a lot of elements in it that have consistency with the Administration's proposal, and, obviously, we would like to work closely with you and the Committee to find ways to address the concerns that have been raised, frankly by both sides of the aisle.

#### GREEN BUILDINGS

Mr. QUIGLEY. Sure. In terms of LEED-certified buildings, by retrofit or by new construction, certainly, is that not a new idea that has been lauded by for-profits, not-for-profits, people in government and outside. Most recently, National Academy of Sciences reaffirmed the value of the Department of Defense using LEED to certify green buildings for taxpayer savings. I learned a long time ago that I was not going to convince a lot of folks to do things like this just for the environmental aspects of it. But given our nation's water shortage, given our nation's desire to reduce pollution, but also to reduce dependence on foreign oil, energy conservation makes a lot of sense. And, of course, there is the financial savings from being efficient. Your views on where GSA is and where it needs to go on LEED certified.

Mr. TANGHERLINI. I think having third-party certification of the work that agencies are doing to improve efficiency is a great way of making sure that you are actually getting the results that you are paying for. And so we have used LEED certification as a way of providing that third-party certification of the work we are doing. We have a notice of proposed rulemakings out right now for comment that is asking the community to consider the possibility of two other certification programs. And our testable hypothesis, if you will, is that an agency should focus around one set of certification so that they can compare their buildings from an apples-to-apples perspective. But, you know, underlying that is an affirmation of what you were saying, that having good, strong certification, making sure you can test those outcomes, that they are repeatable, that you have clear standards, is helpful in making sure that you

are getting the kind of outcomes from the investment that you are guaranteeing the return on that investment.

Mr. QUIGLEY. But the public's benefit, where are you at? As we build new buildings, are they LEED certified?

Mr. TANGHERLINI. Yes, they are.

Mr. QUIGLEY. And as we retrofit, even the buildings we are sitting in?

Mr. TANGHERLINI. Depending on the level of retrofit, we are either moving towards some form of LEED-certification, and GSA has used out LEED as our certifying entity. But more importantly, we are running efforts like a program we call Shave Energy, in which we are constantly going through buildings and asking on a continuous basis, are there ways we can reduce the energy costs? So while we have seen an increase in energy costs over the last 10 years or so of about 32 percent, our costs for providing energy, heating, cooling, lighting of our buildings have only gone up 18 percent. That gap is a direct result of those energy efficiency savings and investments.

Mr. QUIGLEY. And I was going to ask you, to what extent do you document the cost savings and energy savings as you do this?

Mr. TANGHERLINI. Again, it depends on the nature of investment. We document all the savings by collecting all the electric bills and comparing them from year to year. So we have a bottom-line documentation. But in the case of large-scale investments, we have a program we call "The Green Proving Ground," which actually provides scientific analysis, using clear scientific method to evaluate the relative performance of one investment over the other. And then use that to make going-forward decisions on the type of equipment, approaches, designs that we'll use going forward.

Mr. QUIGLEY. Very good. Thank you Mr. Chairman. I yield back.

Mr. CRENSHAW. Thank you. Mr. Graves.

#### CONFERENCES

Mr. GRAVES. Thank you, Mr. Chairman. I would venture to say, Mr. Administrator, that a few years ago many people probably did not know much about GSA. And it reached the headlines, though, of newspapers all across the country, and, really, the lips of so many folks. Just asking the question: How could there be so much abuse within the federal government, within an agency that is actually there to promote responsible management of assets? And, as you know, I am speaking of the conference that took place in 2010 that was not revealed until last year, I suppose. A lot of talk, a lot of promises of reforms and review, and, in fact, even you referenced it, I know, in your statement. You used the phrase here that, "There would have been dozens of meetings with employees and senior agency officials to examine the underlying root causes that led to that conference." I mean, what can you do to reassure us that something like that will not happen again? What has taken place? What process in place? What accountability measures, not only have you, as an agency, done, but would recommend to others as well?

Mr. TANGHERLINI. Well, I think there have been a lot of changes across the federal government as a result of the revelations at the Western Regions Conference. So it makes me a little less popular

when I go see other agencies because a number of clear steps have been taken, such as the review of any conferences over \$500,000 have to be approved by the agency head. Deputy secretaries are now approving any kind of conference, certain levels of travel. It depends on the agency. So we have taken those steps within GSA. But we also recognize that we have kind of a higher bar and a higher order of tasks in order to win back people's trust. So we have taken some additional steps, some of those in coordination with this Committee.

One of things I think that led to the ability for those abuses to happen was a lack of transparency of spending down to the local level. So money was able to be spent and no one was able to monitor it at the headquarters level. We had a chief financial officer in name only. They were not actually in charge of all the finances for the agency. That was one of the steps we took immediately, was consolidating all the CFO activities under a single chief financial officer, so that person would be accountable; so they would have clear interests, desire, and enthusiasm for going and finding out how resources were being spent, and making sure that we had a good solid CFO, the type you would have in any business, whose job it is to ask, "Is that the best way to spend a dollar? Are we going to get the marginal benefit out of that marginal expenditure?"

At the same time, we also looked, as a result of that, asking ourselves where else do we see redundancy within the organization, lack of transparency, and lack of accountability? It is my view that we found that within the chief information officer's office. We had a CIO also in name only. She was not in charge of the over \$700 million we spend every year on investing in IT. We had a chief people officer, or human capital person, who was in charge of only one level of approval, and, as a result, two or three other levels had built underneath him. So one of the lessons we learned was we need to have clearer accountability, we need to have clearer sets of permissions. We need to have stronger transparency and visibility into the way resources were spent. And we need to have stronger accountability. Those are things that we, in some cases, took immediate steps to implement; other cases, we are working towards implementation. Some of those processes are hard. That play is underway right now.

But I look forward to coming back to the Committee and talking about the progress, maybe problems we have identified, and maybe using that as a way to demonstrate to other agencies how they, too, can benefit from our experience.

Mr. GRAVES. Is there a conference planned for this year?

Mr. TANGHERLINI. There are not many conferences planned at all. In fact, just yesterday, we cancelled two additional conferences. Conferences, frankly, have value; we ran those conferences last year. Look, we cancelled 39 conferences over the course of last year. We reduced spending in travel around conferences by over \$10 million. There were a number of conferences, though: The Expo Conference, the Fed Forum, and the Smart Pay Conference, which were entirely about training. Now, I was doubtful. I went down to Expo myself and I said, I have got to take a look at this. I want to see a lot of busy people. If there is a camera crew here, I want



have them see people who working hard, who are learning, who are interacting.

You know, we had hundreds of businesses come. Those businesses invested about \$6,000 or \$7,000 each to come. So they clearly made a business judgment that there was value there. So I was very careful about not getting in the way of that. And I came away impressed. I came away impressed by the fact there were hours and hours of procurement training, procurement law training; making sure that the people who are committing federal dollars are doing it with the latest knowledge, the latest rules, and the latest techniques. That training was provided to the vendors, too, so that they knew how to relate with the federal government.

But this year, you know, simply because of pressure on budgets through sequestration, concern about travel, we just were not having people sign up for the conferences. It started with Expo, which was just before sequestration. And it was clear that we were not going to get enough people down there to make it worthwhile for us to go and have it, and spend the money to do it, or for vendors, frankly, to come. And it then followed up with Fed Forum, which is primarily about fleet management and other asset management. And now Smart Pay, which is really about training on how to better manage the federal credit card programs. I am worried though, that we are going to lose a year of training. So we are working very hard to make sure that training is available via the Web or other means, so that people still get the benefit of it.

Mr. GRAVES. The reports say that as a result of that conference, I mean, reports of scandal, reports of abuse, that 46 individuals were suspended, warned, or reprimanded; 11 terminated. And the 300 who attended received a letter from GSA saying that was not a smart idea. Is that sufficient? Do you think that all those responsible were taken into account in the proper manner, or is there still more that we can expect?

Mr. TANGHERLINI. I think the folks that were directly related to that activity, or we thought had responsibility for that activity that happened, you know, we did take aggressive action against them. Is it possible that there were folks we missed, or there are other people? That is possible. But I tell you, I do consistently meet with the Inspector General. I work very hard to build a strong relationship and partnership with the Inspector General; not one of separation, and now maintaining his independence, but we want to know. If they feel that there is more that we can do managerially, we are going to do everything we can to respond to that.

At the same time, we also want to make clear that our expectations about the way our organization will behave, the expectation of our employees, about what they will do on government time, has completely changed. Now, I will tell you that most of the GSA associates I meet with are very happy with those changes.

Mr. GRAVES. Well, Mr. Chairman, I know my time is out. I want to thank you for taking an aggressive approach to this. It is something that is very important to us as a Committee, and I know that your agency was embarrassed by it, and it was an abuse of taxpayer dollars, so we thank you for your aggressive and serious approach to it.

Mr. TANGHERLINI. I appreciate it.

Mr. CRENSHAW. I just saw on the news that the Post Office had a conference. According to the news account, it spent \$2.2 million having their conference. And if you are losing \$16 billion a year, it all adds up somewhere, so maybe they learned a lesson, or maybe they did not. But we do appreciate what you have been doing. Ms. Herrera Beutler.

#### GREEN BUILDINGS

Ms. HERRERA BEUTLER. Thank you, Mr. Chairman. And I actually wanted to follow up a little bit on the LEED certification. I am from the West. In the West, we have lots of trees. I was looking at your bio. You spent time in Pennsylvania. But mostly, it seems that the life cycle of a tree is something that is very foreign to people here in D.C. It is a very green process, and can be harnessed and utilized. And some of my concern is that with the adoption of some of the LEED standards, we actually are disadvantaging or choosing not to utilize the carbon sequestration that takes place when we use our forest products. And specifically, I had a couple questions. GSA released an addendum that expanded the original study on green buildings on the rating system. That was released last year to include several other systems that had not previously been included in the analysis. Why were those systems that incorporate energy savings and science-based life-cycle assessments, such as the International Green Construction Code, left out of the addendum?

Mr. TANGHERLINI. I am not sure about the specifics, but I think the important point is that we recognize that there is more than one standard now. And what we are doing is working very closely with other agencies, working very closely with the National Science Foundation to try to come up with a set of standards, then, that we would offer agencies to use so that we would begin to give people choice. Now, we are out with a notice of proposed rulemaking, so if people think we have missed something, people think that there is a better approach to this, we actually not only welcome the comments, we are requesting people provide us comments so that we can get this right.

Ms. HERRERA BEUTLER. Well, I am going to guess that some of the folks who contacted me probably have put in comment, and if my office has not, we will as well. One of the systems the GSA is claiming as a consensus standard, which is required under the Energy Independence Act of 2007, your agency acknowledges is not a consensus standard. Even though you put it out for comment, how can you justify this to make sure that the process that you are following respects the spirit and the letter of the law?

Mr. TANGHERLINI. Well, you know, any action we would take would have to reflect both the spirit and the letter of the law. So I think we would want to make sure, again, I do not know the specific issue related to that one standard, but I will follow up with you, I will learn more about it, and try to get back to you with an explanation on how we have a disagreement about why that would qualify and, in some view, maybe should not.

[The information follows:]

OMB Circular A-119 (1998) establishes policies on Federal use of voluntary consensus standards, based on the National Technology Transfer and Advancement

Act. These policies define “voluntary consensus standards bodies” as “domestic or international organizations which plan, develop, establish, or coordinate voluntary consensus standards using agreed-upon procedures. . . .” They also are defined by the attributes of openness, balance of interest, due process, an appeals process and consensus. The NTTAA directs that federal agencies use voluntary consensus standards to carry out their missions; however, the use of other technical standards to meet government needs is not prohibited.

The Green Building Certification System Review completed for GSA in March 2012 concluded that the U.S. Green Building Council’s Leadership in Energy and Environmental Design (USGBC LEED) system was developed as a voluntary consensus standard, based on criteria developed to address the attributes outlined above.

ANSI publishes the Essential Requirements: Due process requirements for American National Standards. This document sets forth the requirements for developing standards which carry the designation of American National Standards. The process for standards developing organizations to demonstrate conformity of individual standards with ANSI’s requirements has two parts. The first is demonstrating that the processes used by standards developers meet ANSI’s requirements. The second is demonstrating that individual standards have been developed in accordance with these processes. Only standards that have gone through the second step can be designated as American National Standards.

Although, USGBC has demonstrated that its processes meet ANSI’s requirements, at the present time, individual USGBC standards have not been designated as American National Standards.

Ms. HERRERA BEUTLER. Well, we can follow up with the specific standard that I am thinking of, but I think, overall, some of our concern, you know, I even heard when you were talking about the third-party system. Another aspect of that is making sure there is not the capture of the third-party system.

Mr. TANGHERLINI. I completely agree.

Ms. HERRERA BEUTLER. And I think that is where some of us in the West, and some of our producers and our small forest land-owners are feeling like there is a group here that maybe needs to come out and tour some of the forests that we have and understand the morbidity of trees and what a benefit they can be in this process. And I would like to follow up with your staff and get some specifics on this because this is a huge issue for the Northwest region.

Mr. TANGHERLINI. And I think we are closer than farther apart in the sense that what we are trying to do is create some options within the standard-setting process, recognizing that there is value to standards.

Ms. HERRERA BEUTLER. Well, and in that I would say in the Northwest, we pride ourselves on being very eco-friendly.

Mr. TANGHERLINI. Right.

Ms. HERRERA BEUTLER. So we manage some of these standards in Washington State, so it seems to me that they should be manageable and there should be some cooperation with the federal standards.

Mr. TANGHERLINI. Okay.

Ms. HERRERA BEUTLER. Thank you. Thank you, Mr. Chairman.

Mr. CRENSHAW. Thank you. Turn to Mr. Womack.

#### GREEN BUILDINGS

Mr. WOMACK. I thank the Chairman. I thank the Acting Administrator for his testimony. I want to pick up on where Jamie was on the standard issue because as I understand the voluntary consensus mandate, it basically says that exceptions to voluntary consensus should be made only when there is a clear violation of appli-

cable law, or whether the standard is impractical to apply. Now, that is kind of the spirit behind the issue. So my understanding is that Green Globes is the only commercial green standard that has been approved by the American National Standards Institute. But yet almost everything is exclusively LEED. So help me through this process. That is not a violation of applicable law; it is not impractical. And we know that Green Globes is a much more affordable standard with which to judge. So help me with this. I am struggling with the mentality that GSA is using in this process.

Mr. TANGHERLINI. Well, no, I think actually we are trying to create the kind of environment that you are discussing in which people can make choices about the standards that apply and diversify the choices from ones we have right now. And that is the whole point of the rulemaking, to say, "Look, we want to diversify the options that agencies have." We think that there is value in having these standards and judging your investments against those standards so that we have some way of calibrating whether the investment returns what we hope it will return. And, as an appropriator, I know you are very interested in that. And we are also saying that it is important that agencies, when they adopt a standard, they maintain some consistency so you can compare it from year to year.

But right now what we do not have is that kind of broader set of standards that people can choose from. Now, it is the specifics of Green Globes versus LEED versus others; that is part of what we are trying to get out through the comment period, trying to understand whether we have picked the right ones, is this the right approach, how do we move forward? The fact is, we are having a conversation at least around the right stuff. And that is, how do we get better data into evaluating the investments that the government makes? Now there are questions about whether you are using the right tools or not. But I tell you, that is progress over the way much of our investment happens. And so I think that if we can find some accommodation, if we can get some benefit from these comments, hopefully we will come up with a system that takes us a little closer to a better outcome.

Mr. WOMACK. But you have been on the job for several months, and I am not asking whether there is universal agreement on the other standards. I am asking for your opinion. Have we gone, have we, I hate to say the word wasted taxpayers' money, but in your opinion, as the Acting Administrator, have we violated some of the spirit of the voluntary consensus by being specific with LEED, in your opinion?

Mr. TANGHERLINI. Well, no. I think that is why we have proposed saying, "Let's provide the possibility for agencies to consider alternatives."

Mr. WOMACK. Reclaiming my time. I am just specifically asking you, as the Acting Administrator, something is driving the rule-making process, and I understand that, but can you defend the LEED certification process versus, say, Green Globes, which is arguably more affordable. We are talking about the expense of taxpayers' dollars here.

Mr. TANGHERLINI. Sure.

Mr. WOMACK. And it is just like the discussion that transpired about conferences: Some conferences are better than other con-

ferences. But I am just asking in this particular case, we have been specific with LEED, have we missed some opportunities to save the taxpayers money? I realize we are looking at it in the future, but in the past, have we?

Mr. TANGHERLINI. Well, that is the point, it was not available in the past, and so I think we have realized tremendous value through using some certification process. I mean, clearly, maybe there is benefit to using one versus another; that is a possibility. But if you are using one versus none, that also could have wasted taxpayer money. So I know in the one instance where I worked with the certification process, using the LEED certification process, to help us get the main Treasury building LEED gold-certified, that we saved money for the Treasury Department. Now the relative cost of LEED versus something else, since it was not an option, I cannot really answer the question. I do know, though, by taking the steps to get that certification and understand how we spent money on energy, what kind of investments we needed to make to reduce our energy intensity, approach different ways to cleaning the building and operating the building, we saved the taxpayers money. So it really depends on what you are looking at and what was available to the people when they were making those decisions. That is why we are trying to provide more competition, more opportunity, but we want to make sure we do it within both the spirit and the letter of the law.

#### CLOUD BROKER

Mr. WOMACK. I look forward to the conversation in the future on this subject. I have got one more question, and that is, I am holding a letter that I sent to your agency on February 12 to you, and asked for a 30-day response on cloud broker activities. And so, specifically, am I going to get a response to this letter, and can you update this Subcommittee on the request for information, and are you moving forward of the concept on cloud brokerage?

Mr. TANGHERLINI. No, I appreciate that, and I apologize that we have not yet responded to your letter. You will get a response; I will ensure that. The whole point behind issuing a request for information was to get at the very questions that you were asking in your letter: Is there value here? Do we believe that having people help agencies make the transition to the cloud can save agencies money? There is concern about does that limit competition, does it create another level of expense within agency contracting? To answer that set of critical questions that you have, the best answer is, "Look, the agencies will get to choose what the right path is to conversion to the cloud." Some agencies might be a little more mature, they might have better skill sets, they might have better understanding of their systems, and so going straight to a cloud solution works for them. In other cases, having a cloud broker solution, someone who could walk them through that process, might have value as well.

But we are still in the RFI phase, which means we are asking for information. We have not done a request for proposals. There is no contract vehicle yet. So I think we are still at the preliminary phase so we can ask and answer the tough questions like the ones you have posed to us.

Mr. WOMACK. Well, as you know, this Committee and the full Committee is always concerned about cost and the layers of bureaucracy that add to the cost. And I know the estimate was a \$20 billion cost of transition to cloud services. And I suppose one of my concerns would be just that layer of bureaucracy and the extreme cost, and maybe the limited interaction that agencies would have with cloud services. And so that is what drives my letter, and it is what drives my concerns on the issue.

Mr. TANGHERLINI. Thank you.

Mr. WOMACK. I appreciate your time. I yield back.

Mr. CRENSHAW. Thank you. And on that issue of timeliness, you know, everybody is pretty busy. And sometimes we get frustrated when responses to our questions are, you know, 30 days or 60 days old. And so we do not expect you to drop everything every time you get asked a question, but I think we would really appreciate it if we could have timely responses, perhaps no more than two or three weeks. Could we agree to work together on that? Because I will have some questions, I know other members will have questions that they will submit for the record.

Mr. TANGHERLINI. And I think if we can have a mutual agreement that we will answer the ones we can when we can. Sometimes the questions are very hard to answer. And in some cases, we do not have the data, we have to find it. So if we could have a continuous dialogue around that, and agree, you know, to get the answers when we get the answers.

Mr. CRENSHAW. Well, I mean, you could just let us know if it is going to be a while, or if you want to give a briefing, then we can have a meeting. We are ready to do all that.

Mr. TANGHERLINI. No, I appreciate it.

#### BUILDING EXCHANGES

Mr. CRENSHAW. We have time for another round of questions. I have one big question that I wanted to ask you about. I have been reading about some of the high-profile property exchanges that you are talking about. I think that there is one out in California, two here in the District. And the one that I have kind of looked at is the FBI building. And so I would applaud you all for trying to utilize the assets we have rather than just asking for more money. But if you are talking about exchange in a big building like the FBI, in downtown Washington, D.C., that is a pretty big deal. Probably multi-year, multi-billion-dollar, multi-party, pretty complicated transaction.

So a couple of questions about that. One, is that something that you all have the in-house capability to assess and deal with? I do not know if you have accomplished any big, high-profile exchanges in the past five or 10 years. Two, is there a need to have any kind of House or Senate approval or prospectus that we would see? And three, how do you assess the value of something like that? Do you do that in-house, or do you have outside consultants? Talk about that because that, I think, if you are moving forward on that, that is a pretty interesting deal, and it is a big deal, and I think it will be high visibility. So I would like to hear how you plan on handling that.

Mr. TANGHERLINI. No, I think those are all reasonable concerns, and we were pretty sure you would have them. But we want to also recognize the interest we have seen from this body, from this Committee, in making sure that we are leveraging our assets and getting the full value of them. We recognize the constraint that the entire United States government is under, this Committee being like my agency, a part of that broader issue of constraint. At the same time, we have exigent, important, and pressing needs to deliver critical services to the American people such as the protection that the Federal Bureau of Investigation affords us. And they are operating in a building in which we are literally throwing good money after bad at this point.

We have reached the end of the useful lifecycle of the building. The building was designed for an agency that served a different purpose in a vastly different time. We have talked to consultants about the quality of the building, how you would renovate the building. We have engaged experts in looking at the structure of the building, the renovation, the ability to renovate the building. GAO has kind of come behind our tracks to make sure that we have used the right assumptions. The FBI has also engaged engineering folks to look at the facility and understand their needs. For the valuation of the building; we have used appraisers, we have used third-party commercial appraisers. It is kind of hard to appraise the value of something like the FBI building. There are not a lot of "comps", as they say in that business. So we have tried to get a sense of what the commercial value is through, for example, the square-foot value of sales in the area.

I tell you, we had some very skilled people within the organization who are focusing on it. We are trying to get the right group of people together who we will not be shy in making sure we retain the best expertise to get the best possible value, because I fully expect to be before this body at some point, and in several points, I would imagine, in this process, explaining how we are maximizing the return of the investment that you made in building that facility to begin with.

We think that there are a couple of steps on the authorizing side. We have a Senate authorization; the House is looking at one as well as a possibility. Whether that is necessary or not, I frankly do not think that is particularly relevant. It is very useful to have a sense of what the Transportation and Infrastructure Committee's interests are in the same way we got a sense from Environment and Public Works. And then the question will be whether we generate enough resources out of the transfer of the building, if that is the approach we take. We have not even settled if that is necessarily the best way to do it. Do we get enough out of it to move the project down? Do we have to come and seek additional resources for you? So those all have question marks next to them. We have not answered them yet.

But I think our imperative was to get off the dime, frankly, and move forward and query the marketplace, see what was out there, see what interest there was. I am happy to report there is an awful lot of interest, 35 different responses to our request for information. We have learned a lot. But then we have to go through a process of trying to distill that and come up with what we think the right

approach is, and then work with this Committee, among others, to make you aware, and get your input and suggestions as well.

Mr. CRENSHAW. Well, thank you. I do not quarrel at all with, you know, this kind of concept because we talked about all the property that we know that we own or we do not own. And I know there is an effort to sell some of the surplus property. But I think if you can exchange a valuable piece of property like that and have a new facility out somewhere that is more secure, and you know, just a better place for people to go to work, and it does not cost any money, shoot, that is what we ought to be doing more often. And so I just want to be sure that as you undertake that, that we do that in an appropriate way because it is, it is a pretty complex transaction. Just selling a piece of property is tough enough, but to actually do exchange, it could be very beneficial to the taxpayers if it is done right. So I appreciate the work that you are doing as you get started, and please keep us abreast of that, if there are things we can do to help. Much rather have you go exchange a piece of property and have a brand new building somewhere than come ask us for some more money to build a building somewhere. So thank you for that. Mr. Serrano.

#### BUILDING CONSTRUCTION

Mr. SERRANO. Thank you, Mr. Chairman. Mr. Administrator, let me talk to you about the impact of the continuing resolutions, the CR, on your agencies. As you well know, it looks like GSA is going to be held at 2012 levels. What is the impact of those decisions, particularly on federal buildings, current projects, and construction jobs? And, in addition, I want to ask you very briefly also, something you dealt with in the past and that is the St. Elizabeth's project. How is that going and how does this impact it?

Mr. TANGHERLINI. Well, no, I think that is a great set of questions and it is one that we are very concerned about because if you think about it, the 2013 levels really built off the 2012 levels, which are, frankly, a CR off the 2011 levels. I think the last time we had an appropriation was 2010, and so we have to guess, we have to work off of those assumptions that were baked in several years ago about agencies rent expectations, about need for maintenance, and, frankly, the last several levels of funding for the organization have really been low in terms of making reinvestments back in the properties that we own, so we just have not had as strong a repair and alteration program.

[The information follows:]

In Fiscal Year 2012, GSA received its appropriations through the Consolidated Appropriations Act of 2012, as opposed to being funded from a continuing resolution based on FY 2011 funding.

We have really had no construction program, other than the Recovery Act program which came in in 2009, and so I think that is a concern that we have. We look to what the business benchmarks are, and the business benchmarks in real estate say you should invest between 2 and 4 percent in your facilities of the fair market replacement value of those buildings, and we have not been, for the last several years, we have not been investing that amount of money. We do know, also, from business benchmarks that \$1 of maintenance and repair obviates the need of \$4 to \$5 of capital re-



placement. And so while we are figuring out ways to keep, you know, the buildings at some level of operational quality right now, what is going to happen three, four, five years down the road is that that lack of investment is going to come back in the form of really dramatic concerns and maybe emergent or exigent concerns: boilers that stop working, roofs that fail. And so this is much like, on a very grand scale, what it is like to be a homeowner, and the fact that you need to continually make investments in your home, recognizing that if you do not, you are going to have very expensive, episodic, you know, step-function costs that you are going to have to come up with ways to pay for it.

On the St. E's project, we have enough resources to get us through opening up the Coast Guard component, but then we fall short on the subsequent phases of that project, and as a result, we are not able to consolidate the dozens of leases that the Department of Homeland Security has around the National Capitol region. We have the Homeland Security suboptimally spread out across the National Capital region. It is costing them money in terms of lease costs, but it is also costing them money in terms of efficiency, the ability to collaborate, and maybe the ability, at some level, to be as effective an agency because they have not been able to fully come together in one headquarters location.

Mr. SERRANO. I mean, that project has been around so long, and do you see something happening?

Mr. TANGHERLINI. Well, I have to say that the fiscal year 13 CR level does not really give us much in the way of resources to move the ball forward. We are trying ideas, such as the Federal Triangle South idea, which is an exchange of several buildings down south of Independence Avenue. One of the buildings involves Department of Homeland Security. Perhaps if we could gain some value out of that exchange, there would be something else we could do to help the Department of Homeland Security, but right now, I just do not see a financing solution for the completion of St. E's.

#### CLOUD COMPUTING

Mr. SERRANO. Let me ask you a question very briefly about an IT issue. I remember a hearing here where then Chairwoman Emerson and I spent a long time talking about the cloud, so we will bring the cloud back for a second. And your agency is a major participant in cloud computing and setting the example for other agencies. We have talked a lot about the cloud with our other agencies, and there are varying levels of comfort with the security of the information sent to the cloud. How has your experience been and how comfortable are you that the information you have shared is absolutely protected?

Mr. TANGHERLINI. Well, I think from a cloud computing standpoint, we, too, are very concerned about information security. I will tell you that they found the fact that we had access to our data through the cloud incredibly valuable during the events of Hurricane Sandy. We had employees who could not get to their federal offices but were able to log into their email, were able to log into our systems because those systems were resident in the cloud. They were not locked into a proprietary kind of network, or system, or structure. Because we are also very interested in helping agen-

cies make that shift, and protecting the security and safety of data, we have a program that we have launched in coordination with the White House called FedRAMP, which allows us to get certification of systems upfront so agencies do not have to go through the arduous process of certifying each individual cloud investment or system that they use.

Mr. SERRANO. Right. One last question on that. We understand that you are responsible for certifying cloud computing software to ease use by other agencies, but that you have had to delay the approval process. What problems are you encountering and how will this affect the federal government's ability to transition to the cloud?

Mr. TANGHERLINI. Well, you are actually speaking about the FedRAMP program. Some of it is that we have just had a huge amount of response of interest of people being certifiers, so getting through that process of certifying the certifiers has been a little more arduous than we assumed.

Mr. SERRANO. So it was not a problem, as such.

Mr. TANGHERLINI. Well, it is a high-class problem at some level but that having been said, we also want to make sure that once certified, we have people that actually are up to the task, can do the work. So I think that, you know, we have got to be thoughtful and we have got to be careful. When we are dealing with something like IT security, you want to make sure you try to hit your deadlines, but you do not want to make the deadlines controlling. You want to make sure that the real controlling outcome that you are going for is IT security.

Mr. SERRANO. All right. Thank you, Mr. Chairman.

Mr. CRENSHAW. Mr. Quigley, do you have any other questions?

Mr. QUIGLEY. No, Mr. Chairman, thank you.

Mr. CRENSHAW. Mr. Serrano, any more questions? Oh, I did not even see you sitting there. All of your friends left.

Ms. HERRERA BEUTLER. All the boys left, Mr. Chairman.

Mr. CRENSHAW. All the boys left. Well, thank you, and I would certainly like you to have a chance to ask any questions you might have.

#### REAL PROPERTY DISPOSAL

Ms. HERRERA BEUTLER. I just wanted to kind of comment and follow-up on what you were saying, and I was kind of trying to assess just where your perspective is at, and I was encouraged when you were talking about the FBI building. The bill that you referenced from the T and I Committee, I was on T and I last year, was basically creating the Citizen Commission that said any time you are going to buy a property, that you sell a property, or that you consolidate. You know, it is a kind of a commonsense measure. You know, I am curious as to how much property is the last, you know, three, four years, since the recession have you downsized in terms of co-location, consolidation, selling? How much are you actually selling?

I know times are tough; you know, you were responding to Mr. Serrano's question about the CR, the levels that we have been at the last couple of years. I would submit for your consideration, I do not know of a corporation, or a small business, or a family in

the last four, five, six years who has not made the same kind of tough decisions. You talked about being a homeowner. People sell things. They get rid of cable. They moved the CEO from a back headquarters into a room with everybody else. I mean, these are real-world examples, and so, yes, you are having to do more with less, but I guess I would argue that now is the time to be innovative and creative with these. And I guess I would like to hear you speak to that a little bit.

Mr. TANGHERLINI. No, I really appreciate that opportunity, and I think that was what I was trying to get at with the opening statement that I frankly think that GSA has, frankly, never been more valuable in our history than right now. Why? Because GSA is really about leveraging the scale and the scope of the federal government to trying buy things once and well, to drive down costs, and to find those places where we have common administrative expenses and try to get some benefit of the scale of them. I can tell you in some very clear, high-profile examples, I think it was just two weeks ago, for \$19.5 million, we sold what we call the Georgetown Heating Plant—a big empty building that was redundant to another steam facility we had—that had been sitting empty for 20 years. We got that out into the marketplace. We had an auction. It was exciting, the bidding; it was eBay on a grand scale. And we had it sold for \$19.5 million.

And the important thing about that is now that is a building that is going to be returned to the economy. There are going to be jobs created rebuilding that building; there are going to be jobs created working for whatever happens in that building. And then there is going to be taxes paid on a building, a building that did not pay taxes before. Look, we are really interested in finding those opportunities; we are committed to pushing forward on them. We have proposed an exchange for services on the 312 Spring Street Courthouse in Los Angeles, California, the idea being to ask someone if they could take this beautiful, historic building that needs pretty substantial seismic retrofit and trade it for a smaller, efficient office space that we could use to reduce rent cost for federal employees. We have asked the marketplace if anyone would help us with the Dyer Courthouse in Miami, Florida.

We have put out a request for information for something we are calling Federal Triangle South. It is six properties including the Cotton Annex Building, the abandoned Cotton Annex Building; it has been empty since 1986. And asking our private sector partners, is there some more efficient way we can house federal employees in the Department of Energy building, which is one of the least effective buildings of federal office buildings we have, which is an ironic thing. I am not going to comment further other than to say we want to help them get a more energy-efficient headquarters building that allows their people to work in a more efficient, high-quality workspace that reflects the work that they do today rather than the work the building was built for in 1970. And then free up, I think it is, three times the usable, developable space that is available there that is unrealized. We are working very closely with the National Capital Planning Commission in the city to try to find ways to do that.

We are looking across the country to find opportunities like that. GSA headquarters itself is going to consolidate two leases into the GSA headquarters. We added a little extra space to headquarters, but what we have really done is reduce dramatically the amount of space that employees have. I am sure you saw that article recently in the paper about the CEO of the Energy Concern who was moved out of a big corner office into his own cubicle. I am glad to say that I am a cubicle companion with that CEO. I looked; his was a little bigger than mine, actually. But the point is to do our work efficiently and effectively, we need to demonstrate efficiency. And GSA is going to lead, and we are going to do whatever we can to help our agency partners who are also committed to those outcomes, get those results as well. I look forward to a partnership with this Committee to help us find, maybe in some cases, those resources we need to make investments. In our 2013 request, we had a request for consolidation money that would allow agencies to make the necessary investments. Sometimes, you know, you have to take down walls or buy new furniture to go from the office to the cubicle.

Ms. HERRERA BEUTLER. On that front, would you be the folks that we would talk to about maybe encouraging the EPA and the IRS to use one television, in-house televisions, and 24-hour satellite studio versus that each having one across the street from each other?

Mr. TANGHERLINI. Well, I think GSA could maybe play a stronger role in helping agencies build that kind of collaboration and cooperation. And I think, at a fundamental level, when I go and I talk to those agency leaders, they are dying for solutions like that. They are looking for answers like that. And so we have got to challenge ourselves to be a bit more aggressive and a bit more effective in identifying those solutions, and bringing them back to the agencies, and trying to find ways that they can realize those outcomes, too. Because as I said earlier, every dollar spent on space you do not need is a dollar that could have been put back into program or returned to the taxpayer. And agencies are feeling that right now.

Ms. HERRERA BEUTLER. Thank you. Yield back.

#### REAL PROPERTY DISPOSAL

Mr. CRENSHAW. Well, thank you. And just on that note, I know that there is a plan, I think, to sell property every year, I think maybe up to 100 properties, and most of them are smaller. But the one that she talked about or you just mentioned, the big one, \$19 million, that kind of high profile, I guess the kind of question is, is why was that sitting there for, I do not know, 15 or 20 years? And are there other properties sitting around? Is that something that you all decided to do just recently, or is that something you have always thought about doing, just never gotten around to do it? Because there has got to be a lot, I think something like 9,600 properties, that there is a plan to dispose of those from time to time. I know, I think our bill had a \$100 billion from consolidation that we never got around to passing. So talk about that, about what are your plans? If you had the \$100 million that we had put

in our spending bill, how would you use that? A lot of little deals, one great big deal, and how is disposal work coming?

Mr. TANGHERLINI. I think we would go with the little deals over the big deals. But what we would like to do is find those with the highest return on investment. Now, there was some language differences we had about the bill, about whether GAO should evaluate the, you know, return on investment analysis, but that is the kind of thing we can discuss and work on. I will say that, at one level, one concern we have about fixing a maximum amount of square footage under the management of GSA costs us the opportunity, maybe, to bring some of the other agency space under GSA so that we can use some of our authorities to better utilize it. So that is something else we can talk about.

But I will tell you this idea of pushing properties out more aggressively, for example the case of the Georgetown Heating Plant. It is a good example that we have to recognize that it is not always that easy to just do it. It seems as simple as putting a house on the market, but any effort that the government undertakes has a huge environmental impact process we have to go through. We have to do a screening to make sure that no other agency wants, or needs, or uses that facility. In the case of the heating plant, we had to make very, very clear that by taking that heating plant capacity offline, we were not jeopardizing the ability to actually heat and cool the federal office buildings. In some cases, there were investments necessary to sever that plant from connections. So we have to recognize that there is a whole spectrum of complexity in moving some of these properties to disposal.

And so working closely with this Committee, I think that we can explore ways that we can make that easier. I think that was the nature of the Administration's proposal around a civilian BRAC, was trying to find ways to streamline that process a bit. But I also think that, you know, looking at agency space, their needs, lease expirations, and asking ourselves, are there targeted investments we can make now to help agencies consolidate space, is the kind of conversation that I think would bear a lot of fruit between GSA, this Committee, and other agencies.

Mr. CRENSHAW. Yeah, I think in these difficult times everybody is part of the belt-tightening, and we appreciate your willingness to be part of that.

Mr. Serrano, you have any final thoughts?

Mr. SERRANO. I really want to thank you for your service, for your work, for the study you've undertaken. At the expense of a bad pun, as we want you to move into the cloud, we want you to remove the other cloud that was hovering over the agency. And it has been a difficult time, and it opened the doors for a lot of attacks. And we have to be honest that so many of the attacks had a base for people to be able to make them. And your mission is a difficult one, but you have the support of this Committee, and I know you have the support of the Chairman. I do not speak for him, but we understand, we both understand the need for your agency to do its job well because then it affects all of us. And so good luck, congratulations, and just whatever you need from us, just let us know. Except for dollars; he is very tight on dollars.

Mr. CRENSHAW. Well, I think we are all working, you know, under some difficult economic times. But I think there is a positive side of that, that makes us all look at ways to do things more effectively, more efficiently. Government always needs money. But right now we need something more, I mean, in terms of discipline and all those kinds of things. So we thank you for what you are doing to try to help restore the reputation that GSA, it got muddied a little bit. I think credibility is important, and I appreciate what you are trying to do. And anything we can do to help you do your job in a more efficient way, we are ready to help. So with that, the hearing will be adjourned.

**Financial Services and General Government Subcommittee**  
**Hearing on the General Services Administration**

**Questions for the Record Submitted by Chairman Ander Crenshaw**

*Green Buildings*

**Question:** How much has GSA paid third-parties for green building accreditations? Please provide a table of the amount paid, the number of accreditations, and the third-party organization for fiscal years 2007-2013 to date, include energy performance programs such as Energy Star. Please identify the street address for each accredited building and whether the building was either new construction or existing at the time of the accreditation. For existing buildings, provide a table of the energy and water consumption and cost three years before and after accreditation.

*Table 1: Green Building Certification Fees\* from FY 2007-2013*

	Green Globes	LEED*	ENERGY STAR
<b>2007</b>			
Number of Certifications		2	9
Total Fees Paid		\$12,847.00	\$0.00
<b>2008</b>			
Number of Certifications		4	26
Total Fees Paid		\$37,557.16	\$0.00
<b>2009</b>			
Number of Certifications	3	6	45
Total Fees Paid	\$16,250.00	\$70,730.02	\$0.00
<b>2010</b>			
Number of Certifications	2	13	76
Total Fees Paid	\$14,800.00	\$74,121.39	\$0.00
<b>2011</b>			
Number of Certifications	2	11	57
Total Fees Paid	\$23,960.00	\$79,124.94	\$0.00
<b>2012</b>			
Number of Certifications		8	82
Total Fees Paid		\$73,219.00	\$0.00
<b>2013</b>			
Number of Certifications		28	15
Total Fees Paid		\$166,762.00	\$0.00
<b>Total Number of Certifications</b>	<b>7</b>	<b>72</b>	<b>310</b>
<b>Total Fees Paid</b>	<b>\$ 55,010.00</b>	<b>\$ 514,361.51</b>	<b>\$0.00</b>

\*Includes registration and certification fees

Please find the following information in the attached tables:

- Listing of buildings with Energy Star, LEED, or Green Globes accreditations, and whether they were new construction or an existing building. (Attachment A)
- Energy and water data for existing GBCS buildings. (Attachment B)

Leaps in innovation can occur with small businesses and new start-up companies. I applaud the administration and GSA for their commitment to small businesses.

**Question: What steps is GSA taking to encourage small businesses and start-ups to compete as green building system providers with LEED?**

GSA is committed to increasing competition in the green building market through local community platforms. By focusing on the promotion of local small business opportunities related to green technologies and processes, sustained economic growth in local communities can be realized. Policy for small business programs with respect to the green building market is under development. Current GSA programs and initiatives include training for small businesses with respect to greenhouse gas inventory and reporting, information on potential subcontracting opportunities for projects such as Energy Savings Performance Contracts, and webinar focus groups for green building market vendors. GSA is partnering with private industrial, commissioning, and trade entities, as well as individual small businesses, to support small business education and participation in sustainable acquisition. Specifically, GSA vendor focus groups view presentations and provide feedback prior to their public release. Vendor benefits include advanced viewing, free education, and insight to possible contracting opportunities. GSA benefits include relevant, understandable informational materials, a larger pool of contractors, and a deeper understanding of green building concepts by vendors.

Congress included a consensus requirement in the Energy Independence and Security Act of 2007.

**Question: Does GSA value consensus standards?**

GSA values voluntary consensus standards. OMB Circular A-119 (1998) establishes policies on Federal use of voluntary consensus standards, based on the National Technology Transfer and Advancement Act (NTTAA). These policies define voluntary consensus standards bodies as "domestic or international organizations which plan, develop, establish, or coordinate voluntary consensus standards using agreed-upon procedures..." Voluntary consensus standards are also defined by the attributes of openness, balance of interest, due process, an appeals process, and consensus. The NTTAA directs Federal agencies to use voluntary consensus standards to carry out their missions, and the use of other technical standards to meet government needs is also allowed.

**Question: And if so, which consensus standards does GSA use now and is it your goal to increase your usage in the future across GSA?**

GSA has adopted standards on health, safety, welfare, and security from the following organizations: American Society of Heating, Refrigerating and Air-Conditioning Engineers (ASHRAE), International Code Council (ICC), National Fire Protection Association (NFPA), Sheet Metal and Air Conditioning Contractors' National Association (SMACNA), Institute of



*Electrical and Electronics Engineers (IEEE), and American Society of Mechanical Engineers (ASME). GSA adopts additional consensus standards as necessary.*

**Question: Under the Energy Independence and Security Act of 2007, is GSA allowed to recommend more than one green certification program?**

*GSA interprets the Energy Independence and Security Act as allowing GSA to recommend one, many, or no green building certification systems to the Department of Energy.*

**Question: Are there advantages to using more than one green certification program?**

*In its findings, the Interagency Ad-hoc Discussion Group, which was co-chaired by GSA, the Department of Defense, and the Department of Energy, felt that agencies should have the flexibility to select the green building certification system that best suits its mission and portfolio needs. However, agencies should be encouraged to use one green building certification system at the agency or service level for internal consistency and to allow for the most efficient use of resources.*

*While each of the three green building certification systems reviewed by GSA is built around a set of standards, metrics, and tools that are intended to define what high-performance means in the design, construction, and operation of buildings, the frameworks developed by the three systems are different in structure and approach, which makes one-to-one comparisons challenging. Using one system at the agency or service level allows the agency to consistently report on its building performance against Federal requirements. In addition, the use of multiple systems at an agency or service level would increase costs related to personnel training and accreditation.*

#### ***World Trade Center Lease***

**Question: Please provide an analysis for the legal basis upon which GSA relied upon to enter into a lease agreement with and obligate funds for the World Trade Center. Identify the specific statutory authorities and provide GSA's interpretation thereof.**

*The signing of the World Trade Center lease was unique, representing the culmination of years of negotiation on a lease arrangement in place of the one halted by the tragic events of September 11, 2001.*

*It is GSA's policy to seek approval of both the House Transportation & Infrastructure Committee and Senate Environment and Public Works Committee before executing a prospectus-level lease.*

#### ***Virtual Employees***

*As of October 1, 2012, GSA was to have reviewed all existing virtual and satellite working arrangements and then every August thereafter. Specifically, the review would determine if such an arrangement was in the best interest of taxpayers and the agency.*

**Question: What was the outcome of the review?**

*The review identified 454 formal virtual and satellite work arrangements within GSA. These arrangements result in a cost savings to GSA of over \$800,000 per year. Most of the virtual and satellite work arrangements involve employees located in areas with lower locality pay rates than the agency worksite. This results in a salary savings of approximately \$1,875,000 per year. These savings more than offset any travel expenses estimated to be approximately \$1 million per year as a result of the virtual and satellite work arrangements.*

**Question: How many arrangements were reviewed?**

*All 454 arrangements were reviewed.*

**Question: How many were allowed to continue?**

*All formal virtual and satellite work arrangements were allowed to continue. GSA put in place controls to manage virtual and satellite work arrangements. We conducted a review of existing arrangements based on those controls, and to date, existing arrangements have continued based on either their cost savings or business benefits to GSA. There is now a process in place to document the cost savings or business benefit for any arrangement, and to assess and approve any new arrangements before they are established.*

**Question: How many were terminated?**

*To date, no arrangements have been terminated as a result of the review. Existing or new work arrangements must comply with the controls put in place to manage travel costs resulting from virtual or satellite work arrangements.*

**Question: How many new arrangements have been proposed, approved, or denied since?**

*Six new arrangements have been proposed and approved.*

**Question: How many arrangements were found to cost the same or less than, up to 10% more than, or more than 10% of the cost would be if the employee were located at the agency worksite?**

*324 arrangements cost the same or less, 127 cost up to 10% more, and 3 cost more than 10% of what the cost would be if the employee were located at the agency worksite.*

**Question: What is the business case for these arrangements?**

*Most arrangements result in a cost savings. Arrangements that represent a cost must identify the benefits to the agency that justify the cost. Typically, such arrangements result in a stronger pool of job candidates or aid in the retention of a highly skilled employee. We also identified mission-related work arrangements that serve as a means to extend GSA's range by locating employees close to some of our customers without incurring the related expenses to maintain office space for one employee. The controls that GSA put in place last year require that all proposed virtual and satellite work arrangements include an assessment of the feasibility of performing the position's functions remotely; the overall cost*

or savings of the arrangement; and, in instances where there is a projected cost, a rationale regarding the benefits of the arrangement. All such arrangements must be approved by the appropriate senior manager.

### ***Property Exchange Authority***

**Question: What statutory authority or authorities is GSA using to conduct the proposed property exchanges for the Los Angeles courthouse, Federal Bureau of Investigation headquarters, and Federal Triangle South?**

GSA has several authorities surrounding exchanges, including 40 USC 581(c)(1), 40 USC 543, and Section 412 of Division H of the FY 2005 Consolidated Appropriations Act (Section 412). The latter authorizes GSA to convey real property and related personal property through sale, lease, exchange, "or otherwise, including leaseback arrangements." Application of a specific authority would be determined by the circumstance.

### ***System for Award Management***

**Question: Has GSA realized any saving from retiring the four legacy systems that were integrated into SAM?**

To date, GSA has not yet realized savings from retiring the four legacy systems (CCR, EPLS, FedReg, and ORCA) integrated into the System for Award Management (SAM). Adjusted for inflation, the four legacy system combined contractor costs total \$10.25 million per year\*, and SAM's FY 2013 estimated costs, including contractors, totals \$13.13 million per year.

\*Note: Analysis adjusts the FY 2010 \$9.69 million in actual legacy contractor costs out three years at the OMB inflation rate of 1.019 percent, to arrive at \$10.25 million.

**Question: How much has GSA spent on the design, development, testing, and deployment of SAM by fiscal year to date?**

GSA has spent nearly \$6.4 million to date since FY 2010 for SAM design, development, testing, and deployment. This includes \$1.62 million in FY 2010, \$3.93 million in FY 2011, \$791,223 in FY 2012, and \$62,377 to date in FY 2013.

**Question: How much has GSA spent on the operations and maintenance of SAM by fiscal year to date?**

GSA has spent nearly \$42.52 million to date since FY 2010 for SAM operations and maintenance. This includes \$9.17 million in FY 2010, \$14.73 million in FY 2011, \$13.14 million in FY 2012, and \$5.63 million to date in FY 2013.

### ***Spring Street Exchange***

GSA announced that it received 10 responses to redevelop Federal Triangle South and 35 responses for the Federal Bureau of Investigation in media reports. Responses were due February 3 and March 4, respectively. Responses to the request for information regarding the 312 Spring Street Facility in Los Angeles were due February 11.

**Question: How many responses did GSA receive for Los Angeles?**

*GSA received four responses to the Request for Information for the Spring Street Courthouse, and is in the process of reviewing them.*

#### *Bonuses as Percentage of Salaries*

**Question: Please provide a table that shows the following: See Table Below**

1. Total salaries paid to Senior Executive Service (SES) and senior-level and scientific and professional employees (SL/ST) in fiscal years 2010, 2011, 2012, and estimated for 2013 for PBS, FAS, and each Other Staff Office;
2. Total salaries paid to non-Senior Executive Service (SES) and senior-level and scientific and professional employees (SL/ST) in fiscal years 2010, 2011, 2012, and estimated for 2013 for PBS, FAS, and each Other Staff Office;
3. Total awards granted to Senior Executive Service (SES) and senior-level and scientific and professional employees (SL/ST) in fiscal years 2010, 2011, 2012, and estimated for 2013 for PBS, FAS, and each Other Staff Office; and
4. Total awards granted to non-Senior Executive Service (SES) and senior-level and scientific and professional employees (SL/ST) in fiscal years 2010, 2011, 2012, and estimated for 2013 for PBS, FAS, and each Other Staff Office.

*SES salaries with award data*

Office	FY 2010	FY 2011	FY 2012	FY 2013 Estimate
Public Building Service	4,309,465	5,565,822	5,000,059	3,328,211
Federal Acquisition Service	4,594,732	5,024,075	5,305,733	4,613,268
Other Staff Offices	8,686,520	9,780,266	9,412,046	9,438,965
<b>Total, GSA</b>	<b>17,590,717</b>	<b>20,370,163</b>	<b>19,717,838</b>	<b>17,380,444</b>
<b>Total, GSA SES Awards</b>	<b>1,313,892</b>	<b>985,910</b>	<b>778,582</b>	<b>102,400</b>

*Non-SES salaries with award data*

Office	FY 2010	FY 2011	FY 2012	FY 2013 Estimate
Public Building Service	620,218,517	626,443,402	593,956,280	551,017,594
Federal Acquisition Service	345,040,205	376,226,509	364,991,380	318,730,437
Other Staff Offices	192,715,835	235,280,795	232,192,615	272,594,044
<b>Total, GSA</b>	<b>1,157,974,557</b>	<b>1,237,950,705</b>	<b>1,191,140,275</b>	<b>1,142,342,076</b>
<b>Total, GSA Non-SES Awards</b>	<b>39,749,243</b>	<b>41,151,453</b>	<b>29,551,158</b>	<b>10,600,000</b>

\* Salaries is defined by Object Class 11, which does not include benefits. Award data does not include the Office of the Inspector General. Please note the source for award data is from GSA's financial system, which tracks all awards by the date expended. GSA award data reported by the Office of the Chief People Officer to OPM is pulled from GSA's human resources system, which tracks awards by the date authorized. When requested, OPM releases a subset of award data that would not match with the financial system.

### ***National Federation of Federal Employees Settlement***

GSA owes \$30 million in back pay to up to 5,000 employees as a result of a settlement with the National Federation of Federal Employees.

**Question: Please provide an estimate of how much of each GSA budget account will be drawn upon to pay the settlement, assuming the decision unchanged.**

As a result of the settlement with the National Federation of Federal Employees, GSA paid \$30 million to up to 4,000 current employees, in addition to former employees, for back pay, damages, and attorney fees and costs. The Federal Buildings Fund and the Acquisition Services Fund are paying over \$27 million of the \$30 million settlement, as the majority of GSA's employees are funded by those funds. The Working Capital Fund is paying approximately \$1.7 million, with the Office of Government-wide Policy, the Operating Expenses account, and the Federal Citizen Services Fund totaling approximately \$1 million.

### ***Takings***

**Question: How many declarations of taking under section 3114 of title 40, United States Code, did GSA file in fiscal years 2009, 2010, 2011, and 2012?**

GSA filed the following declarations of takings: five in 2009; six in 2010; six in 2011; and none in 2012.

### ***Facilities Standards***

**Question: How frequently does GSA update, revise or amend the Facilities Standards for the Public Buildings Service (P-100)?**

Historically, the Public Building Service (PBS) P-100 has been updated every three to five years, with the last update published in November 2010. As an exception, GSA issued dozens of amendments to the P-100 specifically for projects funded by the American Recovery and Reinvestment Act (ARRA) of 2009 to address the high performance requirements.

GSA is currently changing the frequency of P-100 updates from three to five years to quarterly. We anticipate that the new, performance-based version of the standard, will be published late this fiscal year. We are in the final stages of an issuance review which began in the fall of 2012 and received over a thousand comments.

**Question: What is the process for updating, revising or amending the Facilities Standards for the Public Buildings Service (P-100)?**

*Under the current process, PBS' Office of Design and Construction manages the P-100 update, and it undergoes a relatively rigorous internal review before publication. The last P-100 update underwent a rigorous internal review as well as review from outside organizations and individual experts.*

*Currently in draft, the P-100 Manual of Procedures, establishes discipline-specific technical committees, and an overarching steering committee to edit the P-100 on a continuing basis. All amendments and updates will be published quarterly.*

**Question: Who within and outside of GSA participates?**

*Experts within and outside of GSA participate. Under the proposed new process, our internal experts around the country will be largely contributing to the review and edits of the P-100. These experts offer the practical perspective of implementation and variation in geographic and climatic conditions.*

**Question: Is the process open to public comment?**

*The public will be welcomed to comment. We are currently developing a new process by which comments can be received and reviewed.*

**Question: Does GSA test, certify or approve specific building materials to meet the Facilities Standards for the Public Buildings Service (P-100)? If so, what is the process?**

*In general, GSA leaves the testing and certifying of materials to the industry groups that focus on testing and certification. GSA only tests the performance of assemblies, such as facade designs, to assure their capabilities in blast, air-tightness, thermal performance, and constructability.*

**Question: Does GSA test, certify or approve specific building materials for any purpose? If so, what is the process?**

*GSA does not test or certify individual building materials.*

***Buy America Act***

For years, the Financial Services and General Government (section 615, division C, P.L. 112-74) has included a general provision providing exempting the Federal acquisition of commercial information technology from the Buy America Act.

**Question: Why is the provision necessary?**

*The provision recognizes the reality of today's information technology (IT) supply chain—a supply chain that relies increasingly on components manufactured globally and where the U.S.*

Government does not solely drive demand. It allows access to IT products that are difficult, if not impossible, to acquire as domestic end products as well as allowing access to innovative technologies critical to maintaining competitiveness.

**Question: What is the impact on information technology procurements if this provision is no longer included?**

Without this provision, agencies could find it very difficult, and in some cases impossible, to locate commercially available IT products under the trade agreements threshold that meet the tests of the Buy American Act. Meeting the component test for commercial IT that is not "commercial-off-the-shelf" could be burdensome for contractors and disproportionately so for small businesses that are more likely to rely on lower dollar awards where the restrictions of the Buy American Act are not waived by trade agreements.

**Question: Does the purchase of nondomestic information technology increase the Federal government's vulnerability to cyber attacks?**

Purchasing IT from any source carries risk. These risks exist for a variety of reasons; they are not solely the result of a global supply chain. For instance, counterfeit items, malicious code, hardware trojans, or even poor manufacturing and software development practices pose risks to both the public and private sectors, whether the risks originate from foreign or domestic sources. Understanding the application and environment for a given product – including nondomestic IT – is essential to managing risk in a global supply chain.

**Question: What processes are in place to address information technology supply chain risks?**

The Federal Acquisition Regulation requires agencies to address security considerations during acquisition planning and comply with IT security requirements in the Federal Information Security Management Act, OMB's implementing policies, and guidance and standards from the Department of Commerce's National Institute of Standards and Technology. GSA is actively engaged with its interagency and private sector partners to address the rapidly evolving cybersecurity environment. Under Executive Order 13636, Improving Critical Infrastructure Cybersecurity, GSA and the Department of Defense, have specific responsibility for acquisition related cybersecurity recommendations. GSA is also providing support for Presidential Policy Directive 21 to strengthen and maintain secure and resilient critical infrastructure.

## **Questions for the Record Submitted by Congressman Jo Bonner**

### ***Mobile Courthouse***

Our courthouse in Mobile, Alabama has been identified by AOC for years as having been their top priority for replacement. It is plainly unsafe, but action to replace it has been delayed for years.

**Question: Will you commit to working with local judges to find a solution as quickly as possible?**

*As GSA works through the process of defining more detailed project parameters for construction of an annex in conjunction with alteration of the John A. Campbell Courthouse, we will continue to engage both the local court and the Administrative Office of the U.S. Courts.*

GSA's mission is to serve its clients; in this case, the Judiciary.

**Question: How would you rate your own agency's customer service in this case?**

*GSA's renewed mission is to deliver the best value in real estate, acquisition, and technology services. As a part of this mission, we seek to serve our partners within the government, including the Judiciary.*

*For many years, the Judiciary's Five-Year Courthouse Project Plan included a project to construct a new courthouse in Mobile. The Judiciary's Plan for FY's 2013-2017, which reflects priorities approved by the Executive Committee for the Judicial Conference of the United States in February 2012, includes Mobile as its top priority for construction appropriation. Design for this new courthouse, originally funded in FY 2002, was complete in FY 2004. Due to the Judiciary's moratorium on new courthouses from 2004 through 2006, the construction for this project was put on hold.*

*GSA is working to meet the Courts' current needs in the most cost-effective manner possible, while also ensuring that any plan meets new sharing requirements of the Courts and makes full use of the existing historic Mobile Courthouse. We believe that renovation with the addition of an annex will support of the local court, the Administrative Office of the US Courts, and Congress.*

*The new plan in Mobile proposes alteration of the existing, historic Campbell Courthouse to work in conjunction with a smaller adjoining courthouse annex in lieu of the originally planned standalone courthouse. This plan will save taxpayers more than \$100 million from what was originally envisioned and provide a safe and secure facility.*

*GSA's FY14 budget request includes funding for the renovation of Campbell.*

**Question: Would you provide to the subcommittee a list of current new construction of federal buildings, including courthouses, land ports of entry, and other federal buildings, along with cost and amounts appropriated and obligated for each?**

*See attached list of active capital projects. (Attachment C)*

***Travel and Tourism***

Recent news reports indicated a GSA official that was fired in connection with the conferences scandal has been rehired. I think you'll agree with me that it looks very bad for the GSA, and the government as a whole, when a GSA official fired in connection with the lavish conferences thrown with taxpayer dollars is given his job back.



**Question: What is the GSA doing to ensure it does not again become a symbol for wasteful government spending and disregard for fiscal responsibility?**

*Under new leadership, the Acting Administrator has made clear that wasteful spending will not be tolerated. One of Acting Administrator Tangherlini's first actions was to initiate a top to bottom review of the entire agency that examined every aspect of how GSA operates and led to a series of common sense internal reforms that have improved oversight, increased transparency, and enabled GSA to achieve significant savings over the past year.*

*The top to bottom review revealed several issues within the agency, including difficulties with coordination, widespread duplication of support services and investments, and variable performance throughout the agency. In response, GSA is consolidating key support functions within the offices of the Chief Information Officer, the Chief Financial Officer, Chief People Officer, and the Chief Administrative Services Officer. Through consolidation, GSA has realigned to allow our business units to focus on core missions, eliminate redundancies, and increase efficiency, transparency, oversight, and management. In addition, GSA has clarified its regional management structure, strengthened Regional Administrators' authorities, and empowered the Senior Procurement Executive to suspend or terminate procurement warrants.*

*Specifically on conferences and travel, GSA has taken several actions to improve accountability around conferences, travel, and spending in general. GSA established new internal policies for conferences and travel approval. These policies require that employees consider virtual alternatives to conferences and travel such as video conferencing. When alternatives are not suitable, all events must be mission-related, use government facilities if possible, and eliminate wasteful spending. To ensure accountability, all GSA sponsored conferences and similar events must be approved by the Chief Administrative Services Officer and, depending on the cost of the conference, the Deputy Administrator or Administrator. Travel has been restricted to business travel and essential training, and requires the approval of the Heads of a Service or Staff Office or Regional Administrator. In line with the Administration's policies, we also have provided greater transparency into our conference expenses. All approved, agency-sponsored conferences held last year with a cost of over \$100,000 have been posted on a publically available website.*

*All employees are empowered to be vigilant and help prevent misuse of taxpayer dollars. GSA trained event coordinators within the agency on how to prepare and submit requests for approval to host events such as conferences, award ceremonies, and internal management meetings. In addition, GSA developed a mandatory training course for all employees on attending conferences, including events not hosted by GSA. The course helps employees: understand what constitutes efficient spending; make a business decision on whether or not to attend a conference; obtain management permission for attending a conference; understand the best way to make arrangements at low cost; and understand ethics rules on accepting meals and gifts. The course is posted on GSA's training platform, GSA Online University, allowing the agency to track compliance and send reminders to employees to ensure everyone receives this valuable training.*

*GSA's wasteful spending of taxpayer dollars on lavish and unnecessary conferences has cast a dark shadow over all government travel.*

**Question: What can GSA do, and what is GSA doing, to fix the damage they have done to the ability of federal employees to travel legitimately and responsibly in the course of their work?**

*GSA's new internal travel policies are meant to ensure that taxpayer dollars are spent wisely and efficiently. At no point did GSA halt travel for essential business related activities, such as building inspections, contract reviews, and conducting onsite-monitoring visits. GSA implemented new oversight and approval processes to ensure that all travel was essential and mission related. GSA will continue to diligently monitor travel and conference spending. Under GSA's new centralized process, there are multiple levels of approval, justification, and budget requirements that must be met before any conference travel can be approved. Our Chief Administrative Services Officer is responsible for initial oversight and monitoring of conferences and associated travel.*

*In addition, as part of OMB Memorandum-12-12 "Promoting Efficient Spending to Support Agency Operations", GSA and the Department of Defense (DoD) are conducting a review of the Joint Federal Travel Regulation (JFTR) and the Federal Travel Regulation (FTR) to ensure that those policies reduce travel costs without impairing the effective accomplishment of agency missions. In support of this review, GSA has established the Government-wide Travel Advisory Group (GTAC), comprised of industry and government travel experts, to examine government-wide travel regulations and issue recommendations on how to increase travel efficiency and effectiveness, reduce costs, promote sustainability, and incorporate industry best practices.*

It is clear that as a customer-service oriented agency, GSA should spend time with clients, and often GSA's clients are out in the field, not in Washington, DC.

**Question: Recognizing that GSA has rightly restricted travel and related expenses in response to well-publicized scandals at the agency, at what point do restrictions on travel become counterproductive?**

*GSA has limited travel to mission essential activities so as not to interfere with its mission. GSA serves many clients and partners in real estate, acquisition, and technology services. Restrictions have not been implemented that would greatly burden our ability to meet with GSA customers, the public, or vendors, or access certification and training opportunities.*

**Question: How should GSA balance maintaining the necessary checks and restraints on excessive travel with the need to be present at agency projects and properties across the United States?**

*GSA is already striking a balance with a centralized process and multiple levels of approval, justification, and budget requirements for both travel and conferences. GSA employees can travel to conduct mission furthering activities on behalf of GSA as well as for meetings, training, or conferences which are essential to our Agency's mission while the Agency maintains strong oversight over spending and attendance at such events.*

### **LEED/Green Buildings**

The GSA Ad-Hoc Committee recommendations released on February 5 include the need to improve life cycle impacts. I applaud GSA for recognizing the value of life cycle assessment as a science based evaluation of the environmental impacts of a product or material. Green Globes currently uses a life cycle assessment approach to evaluating building material choices, whereas LEED currently does not.

**Question: Why is GSA currently using a rating system that ignores this important science?**

*Life cycle assessment (LCA) is a complex process that is not yet widely used in the U.S. or the rest of North America. Organizations take different approaches to the practical application of LCA because a full analysis of the environmental impacts of products is costly and time consuming. Several organizations (both Federal and private) are developing tools to enable a more widespread use of this evaluation methodology. The lack of consensus about which impact categories to include, and the relative lack of rules for collection of product data are a challenge for advancing the consistent use of LCA in standards. LEED 2009, which GSA currently uses to measure achievement, includes credit weightings based on 13 environmental impact categories for LCA identified by the Environmental Protection Agency. More points are awarded for strategies that have greater positive impacts addressing priority issues – energy efficiency and carbon dioxide reductions.*

The government wouldn't award all its defense contracts to one airplane manufacturer or ship manufacturer; competition among providers brings costs down, spurs innovation, improves product performance. Each manufacturer is competing to serve the government's needs better.

**Question: What steps has GSA taken to ensure that same approach here, and avoid outcomes where all the awards for green building systems essentially get awarded to one provider?**

*GSA is currently conducting its statutorily-required review of green building certification systems. Since GSA first recommended the U.S. Green Building Council's Leadership in Energy and Environmental Design (LEED) to the Secretary of Energy in 2007, much has changed in the green building industry with the creation of additional green building certification systems and tools. GSA plans to submit its recommendations to the Department of Energy later this year on what green building certification system(s) the government should use that would encourage a comprehensive and environmentally sound approach to certifying green Federal buildings.*

The administration knows that leaps in innovation can occur with small companies and start-ups as well as established, market dominant companies. Both the administration and GSA have repeatedly reinforced their commitment to small business.

**Question: What steps is GSA taking to encourage small businesses and start-ups to compete as green building system providers with LEED?**

*GSA is committed to increasing competition in the green building market through local community platforms. By focusing on the promotion of local small business opportunities*

*related to green technologies and processes, sustained economic growth in local communities can be realized. Policy for small business programs with respect to the green building market is under development. Current GSA programs and initiatives include training for small businesses with respect to greenhouse gas inventory and reporting, information on potential subcontracting opportunities for projects such as Energy Savings Performance Contracts, and webinar focus groups for green building market vendors. GSA is partnering with private industrial, commissioning, and trade entities, as well as individual small businesses, to support small business education and participation in sustainable acquisition. Specifically, GSA vendor focus groups view presentations and provide feedback prior to their public release. Vendor benefits include advanced viewing, free education, and insight to possible contracting opportunities. GSA benefits include relevant, understandable informational materials, a larger pool of contractors, and a deeper understanding of green building concepts by vendors.*

**Question: Have any LEED staff or members ever attended or participated with GSA at any GSA retreat, conference, or workshop?**

*To our knowledge, no LEED staff or members have ever attended or participated with GSA at any GSA retreat, conference, or workshop.*

**Question: Were other ratings systems representatives invited to attend?**

*To our knowledge, no other rating systems representatives were invited to attend any GSA retreat, conference, or workshop.*

### **Questions for the Record Submitted by Congressman Tom Graves**

I was pleased to see your agency making some progress on its review of green building rating systems with the request for information on February 5. I look forward to GSA moving forward expeditiously on this effort, and receiving an update when the GSA makes their determination this summer. The study conducted by the Department of Energy clearly shows that both LEED and Green Globes met most of the federal building requirements – with Green Globes performing slightly better for new construction and LEED performing slightly better for existing buildings.

**Question: Given the performance of these two systems, why does GSA suggest that only one system should be chosen by an agency or service?**

*In its findings, the Interagency Ad-hoc Discussion Group, which was co-chaired by GSA, the Department of Defense, and the Department of Energy, felt that agencies should be encouraged to use one green building certification system at the agency or service level for internal consistency and to allow for the most efficient use of resources. While each of the three green building certification systems reviewed by GSA is built around a set of standards, metrics, and tools that are intended to define what high-performance means in the design, construction, and operation of buildings, the frameworks developed by the three systems are different in structure and approach, which makes one-to-one comparisons challenging. Using one system at the agency or service level allows the agency to consistently report on its building*

performance against Federal requirements. In addition, the use of multiple systems at an agency or service level would increase costs related to personnel training and accreditation.

**Question: Doesn't this have a negative effect on open competition and innovation in the marketplace while potentially increasing costs?**

GSA believes open competition and innovation already exists in the current marketplace. In the Federal sector, some agencies such as the Department of State and the Department of Veterans Affairs have been using Green Globes while other agencies such as GSA and the Department of Defense have been using LEED. The findings from the Interagency Ad-hoc Discussion Group did not state that all agencies had to use the same green building certification system. The findings stated that agencies, internally, should be encouraged to use one green building certification system at the agency or service/bureau level for internal consistency and to allow for the most efficient use of internal resources.

I am concerned that GSA is ignoring the consensus requirement written in the "Energy Independence and Security Act of 2007" in your use of LEED as GSA's singular green building rating system.

**Question: Can you tell me what steps GSA will take to ensure the government is only supporting consensus standards as directed by Congress?**

OMB Circular A-119 (1998) establishes policies on Federal use of voluntary consensus standards, based on the National Technology Transfer and Advancement Act (NTTAA). These policies define voluntary consensus standards bodies as "domestic or international organizations which plan, develop, establish, or coordinate voluntary consensus standards using agreed-upon procedures..." Voluntary consensus standards are also defined by the attributes of openness, balance of interest, due process, an appeals process and consensus. The NTTAA directs Federal agencies to use voluntary consensus standards to carry out their missions, and allows the use of other technical standards to meet government needs. GSA will continue to follow the policies established by OMB Circular A-119.

One of the systems GSA is claiming is a consensus standard openly acknowledges that it is not a consensus standard.

**Question: How can you justify this and make sure that your process follows the letter and the spirit of the law? Of the three systems GSA is considering, only one is a full consensus American National Standard (Green Globes). The US Green Building Council's LEED system, has failed to become an ANSI standard and the Living Building Challenge openly acknowledges that it is not a consensus standard.**

In GSA's green building certification system review, initially over 160 tools and certification systems were identified in the current marketplace. Undertaking a detailed review of this large field of potentially useful tools was not cost-effective, so GSA developed a set of screening criteria to narrow this field. To identify which systems met the minimum expectations of a green building certification system with respect to the Energy Independence and Security Act, the following screening criteria were used:

- Systems must employ whole building evaluation, addressing key sustainable design and operations metrics;
- Systems must be available in the U.S. market, and
- Systems must have third party certification.

Three certification systems passed the screening criteria: Green Building Initiative's (GBI) Green Globes® (2010), U.S. Green Building Council's (USGBC) Leadership in Energy and Environmental Design® (2009), and the International Living Building Institute's Living Building Challenge™ (2011). Following screening, these three systems were then evaluated against a list of detailed criteria, which included whether the green building certification system was a consensus standard, per OMB Circular A-119. In our evaluation, GSA acknowledged that the Living Building Challenge was not a voluntary consensus standard.

GSA's evaluation also concluded that LEED and Green Globes were developed as voluntary consensus standards. ANSI publishes the Essential Requirements: Due process requirements for American National Standards. This document sets forth the requirements for developing standards that carry the designation of American National Standards. The process for standards developing organizations to demonstrate conformity of individual standards with ANSI's requirements has two parts. The first is demonstrating that the processes used by standards developers meet ANSI's requirements. The second is demonstrating that individual standards have been developed in accordance with these processes. To be designated as American National Standards, the standards must have gone through the second step.

Although USGBC and GBI have demonstrated that their processes meet ANSI's requirements, currently, individual USGBC and GBI standards are not designated as American National Standards.

**Question: In an era of a \$16 trillion debt and the sequester do you think there are ways that the Federal Government can improve energy efficiency and build green buildings without paying for the US Green Building Council's LEED plaques?**

Green building certification systems have been identified as useful tools to document, track, and report on a building's progress toward meeting Federal requirements. Although GSA's current green building certification system review found that no currently-available certification system ensures that a building will meet all Federal sustainable design requirements (once certified), the Interagency Ad-hoc Discussion Group felt that the use of green building certification systems is a more efficient use of government resources because it eliminates the cost to the Government of developing its own standards.

The Committee agreed upon report language last year that noted "GSA's current green building policies and practices are tailored to reflect the standards of a specific third-party certifications system rather than the public interest in greater energy and water efficiency." It appears GSA is sacrificing building performance and cost to meet the goals of third party systems that have nothing to do with federal priorities like energy efficiency and reducing costs to taxpayers.

**Question: Did GSA consider last year's Committee-passed report language on green building rating systems and what best serves the public interest in this issue?**

GSA's policies and practices are tailored to promote high performance green buildings to meet the aggressive statutory requirements and administration goals on improved energy efficiency, reduced water use, and reduced greenhouse gas emissions. Green building certification systems are just one tool that GSA can use to deliver better value and savings to the taxpayer and meet Federal green building performance requirements. When these systems are used, GSA provides specific guidance on the types of credits that are worthwhile based on their attenuation to meeting Federal green building requirements. GSA's priority is to meet the Federal green building performance requirements contained in law and executive order. To accomplish this, GSA relies on many diverse third parties for standards, and determines the government's needs based on analysis of the purpose of the facility, and comprehensive review of the best practices of the many engineering, architectural design, and operations professions involved.

**Question: It seems no changes have been made to address the 'capture' of GSA by a single third party - has GSA taken any internal steps to respond to the Committee's direction from FY13 that "All agencies should be wary of becoming captured; no third-party certification program has a monopoly on how to attain efficiency, much less sustainability." ?**

GSA and other Federal agencies use green building rating systems as a measure of performance. The specifications used in contracts set the requirements for what is to be constructed. GSA's requirements, for example, are contained in its Facilities Standards. The Facilities Standards rely on multiple codes and standards, including the American Society of Heating, Refrigerating and Air-Conditioning Engineers (ASHRAE 90.1, required by statute), National Fire Protection Association (NFPA), International Code Council (ICC), Institute of Electrical and Electronics Engineers (IEEE), Illuminating Engineering Society of North America (IESNA), Sheet Metal and Air Conditioning Contractors' National Association (SMACNA), American Society of Civil Engineers (ASCE), and American Society of Mechanical Engineers (ASME). These are designed to ensure that the government's requirements for functionality, longevity, safety, energy and water efficiency, security, and healthfulness are met. No one-third party source addresses all the government's requirements. The Facilities Standards have been modified to incorporate new requirements 35 times since 2000, including two comprehensive revisions to every section. Thus the GSA relies on many diverse third parties for standards, and determines the government's needs based on analysis of the purpose of the facility, and comprehensive review of the best practices of the many engineering, architectural design and operations professions involved.

### ***NASA Properties (PBS)***

At a recent oversight hearing before the Commerce, Justice, and Science Subcommittee, NASA Inspector General Paul K. Martin testified that "NASA is the ninth largest Federal Government property holder, controlling approximately 4,900 buildings and structures with an estimated replacement value of more than \$30 billion. In addition, more than 80 percent of the Agency's facilities are 40 or more years old and beyond their design life. Under its current policy, NASA is required to maintain these facilities either in an operational status or, if they are not being used, in sufficient condition that they do not pose a safety hazard. However, NASA has not been able to fully fund required maintenance costs for its facilities and in 2012 estimated its deferred maintenance costs at \$2.3 billion. One way NASA could reduce its facilities maintenance costs is to reduce the amount of unneeded infrastructure in its inventory. To be successful in this effort,

NASA must move beyond its historic “keep it in case we need it” approach of managing its facilities. In an audit issued last month, the OIG identified 33 wind tunnels, test stands, thermal vacuum chambers, airfields, and launch-related facilities that NASA was not fully utilizing or for which Agency managers could not identify a future mission use. These facilities cost the Agency more than \$43 million to maintain in FY 2011 alone.”

**Question: To what extent is the GSA involved in the oversight of this issue, and are you in agreement with their recommendations for cutting costs?**

*GSA works closely with NASA on a wide range of or real estate issues. GSA and NASA are utilizing realty authorities included in GSA's "Property Act", NASA's "Space Act", and "The National Historic Preservation Act". GSA and NASA are working to develop stronger analytics (utilization studies, targeted asset reviews, market studies, appraisals, etc) designed to inform realty strategies. Currently, GSA and NASA are working on outleases, sales, and transfers of many NASA holdings that are not meeting current NASA needs. These transactions will assist NASA in the more efficient operation of their real estate portfolio.*

### **Questions for the Record Submitted by Congressman Kevin Yoder**

#### ***No-Cost Contracting Models***

In your (the GSA's) testimony (p. 2), you state that you are focused on helping “agencies save money on a wide range of support activities so they can focus on their core mission.” One of the ways agencies can focus on their core mission and save money is by making use of the no-cost contracting model. The model is currently used by the U.S. Department of Transportation, Federal Motor Carrier Safety Administration, to manage the Pre-Employment Screening Program, or 'PSP'. The online system makes driver safety records securely and instantly available to trucking companies. A contractor manages all aspects of the system in close partnership with US DOT. The contractor is paid by the trucking companies that elect to use the system. US DOT pays nothing to the contractor to provide services, and the contractor has to meet and maintain compliance with applicable government security and privacy requirements. Over 1.6 million requests for driver records have been completed. FMCSA's Administrator, Anne Ferro, recognized the program's one-year anniversary and stated that "these results show that carriers welcome PSP as an essential tool for making informed hiring decisions that lead to safer drivers on our roads...we know that the majority of our nation's carriers and drivers strive to operate as safely as possible. PSP makes their jobs a lot easier."

**Question: Given the success of the no-cost contracting model at the DOT, how will the GSA look incorporate this model more broadly, to give government agencies access to this type of savings for e-government services?"**

*GSA actively seeks to provide services to agency customers in the most cost effective means possible. An example of such a service is the GSA Smartpay® program. The Smartpay charge card program allows agency customers to realize contracting efficiencies by streamlining the payment process and earn performance based refunds funded through fees collected by the issuing banks from participating merchants.*



GSA conducts market research and reviews industry and government best practices to ensure awareness of innovative contracting models that enable GSA to minimize or eliminate the cost of providing e-government services and maximize the efficiencies realized. As part of our regular and ongoing effort to reduce the cost of providing government services, we will consider your suggestion.

**Question: Could the contractor could simply pay the GSA funding fee based on each transaction completed, or at regular intervals based on the revenues generated from the online service?**

GSA uses various means to collect fees associated with our current acquisition programs. For the largest and most visible, the Multiple Award Schedule program, fees are remitted to GSA each quarter based on contractor sales under their Schedule contracts. Funding mechanisms for new programs GSA develops in the future will be determined on a case-by-case basis, depending on the specific nature of the programs they support.

### **Questions for the Record Submitted by Congressman Steve Womack**

#### ***Green Building Standards***

OMB Circular A-119 requires federal agencies to use voluntary consensus standards. Green Globes is the only commercial green building standard approved by the American National Standards Institute (ANSI), yet GSA has relied almost exclusively on LEED certification for its buildings.

**Question: Explain why GSA is disregarding this administrative policy concerning the use of consensus standards.**

OMB Circular A-119 (1998) establishes policies on Federal use of voluntary consensus standards, based on the National Technology Transfer and Advancement Act (NTTAA). These policies define voluntary consensus standards bodies as "domestic or international organizations which plan, develop, establish, or coordinate voluntary consensus standards using agreed-upon procedures..." Voluntary consensus standards are also defined by the attributes of openness, balance of interest, due process, an appeals process, and consensus. The NTTAA directs Federal agencies to use voluntary consensus standards to carry out their missions, and allows the use of other technical standards to meet government needs.

- The Green Building Certification System Review completed for GSA in March 2012 concluded that the U.S. Green Building Council's (USGBC) Leadership in Energy and Environmental Design (USGBC LEED) system and Green Building Initiative's (GBI) Green Globes were developed as voluntary consensus standards, based on criteria developed to address the attributes outlined above.
- ANSI publishes the Essential Requirements: Due process requirements for American National Standards. This document sets forth the requirements for developing standards which carry the designation of American National Standards. The process for standards developing organizations to demonstrate conformity of individual standards

with ANSI's requirements has two parts. The first is demonstrating that the processes used by standards developers meet ANSI's requirements. The second is demonstrating that individual standards have been developed in accordance with these processes. To be designated as American National Standards, the standards must have gone through the second step.

- Although USGBC and GBI have demonstrated that their processes meet ANSI's requirements, currently individual USGBC and GBI standards are not designated as American National Standards.

**Question: Explain what steps GSA will take to ensure the government is only supporting consensus standards.**

OMB Circular A-119 (1998) establishes policies on Federal use of voluntary consensus standards, based on the National Technology Transfer and Advancement Act (NTTAA). These policies define voluntary consensus standards bodies as "domestic or international organizations which plan, develop, establish, or coordinate voluntary consensus standards using agreed-upon procedures..." Voluntary consensus standards are also defined by the attributes of openness, balance of interest, due process, an appeals process and consensus. The NTTAA directs Federal agencies to use voluntary consensus standards to carry out their missions, and the use of other technical standards to meet government needs is also allowed. GSA has and will continue to follow the policies established by OMB Circular A-119.

As you know, GSA picks the ratings systems the government will use for green buildings, and it has chosen LEED largely to the exclusion of competing systems. We all understand that competition among providers is important; it brings down costs, spurs innovation, and improves product performance.

**Question: What steps is GSA taking to avoid outcomes where all of the awards for green building systems get awarded to one provider?**

GSA is following the NTTAA, as that statute sets forth the way in which the government should use consensus standards. In doing so, GSA is seeking and applying guidance from the National Institute of Science and Technology, designated in the Act as the entity to provide advice to other agencies in the Federal government.

**Question: What steps is GSA taking to encourage small businesses and start-ups to compete as green building system providers with LEED?**

GSA is committed to increasing competition in the green building market through local community platforms. By focusing on the promotion of local small business opportunities related to green technologies and processes, sustained economic growth in local communities can be realized. Policy for small business programs with respect to the green building market is under development. Current GSA programs and initiatives include training for small businesses with respect to greenhouse gas inventory and reporting, information on potential subcontracting opportunities for projects such as Energy Savings Performance Contracts, and webinar focus groups for green building market vendors. GSA is partnering with private industrial, commissioning, and trade entities, as well as individual small businesses, to support small

*business education and participation in sustainable acquisition. Specifically, GSA vendor focus groups view presentations and provide feedback prior to their public release. Vendor benefits include advanced viewing, free education, and insight to possible contracting opportunities. GSA benefits include relevant, understandable informational materials, a larger pool of contractors, and a deeper understanding of green building concepts by vendors.*

[illegible]







## Energy and Water Data for GBCS Certified Existing Buildings

	Energy Use Intensity (btu/gsf)	Total Energy Consumption (btu)	Energy Cost (cost/ /gsf)	Total Energy Cost	Water Use Intensity (gal/gsf)	Total Water Consumption (gal)	Water Cost (cost/gsf)	Total Water Cost
<b>CA0083ZZ</b>								
2007	2,748	201,111,812	\$ 0.15	\$ 10,611	0.13	9,513	\$ 0.03	\$ 2,342
2008	30,883	2,260,017,208	\$ 1.41	\$ 103,477	0.28	20,480	\$ 0.02	\$ 1,244
2009	30,122	2,204,299,420	\$ 1.19	\$ 87,231	0.10	7,318	\$ 0.02	\$ 1,317
2010	26,836	1,953,647,503	\$ 1.18	\$ 86,426	0.24	17,563	\$ 0.02	\$ 1,537
2011	29,215	2,137,925,892	\$ 1.25	\$ 91,768	0.24	17,563	\$ 0.02	\$ 1,610
2012	29,177	2,135,172,128	\$ 1.17	\$ 85,913	0.24	17,563	\$ 0.02	\$ 1,610
2013 (partial year)	14,475	1,059,295,136	\$ 0.58	\$ 42,079	0.10	7,318	\$ 0.01	\$ 732
<b>CA0154ZZ</b>								
2010	58,930	84,150,479,049	\$ 1.35	\$ 1,920,614	13.88	19,820,169	\$ 0.21	\$ 294,161
2011	63,295	90,382,708,140	\$ 1.31	\$ 1,863,486	4.75	6,782,833	\$ 0.07	\$ 102,814
2012	55,389	80,521,217,783	\$ 1.07	\$ 1,532,208	4.36	6,511,328	\$ 0.08	\$ 107,097
2013 (partial year)	24,851	35,486,711,498	\$ 0.43	\$ 608,866	2.18	3,112,966	\$ 0.04	\$ 97,119
<b>CA0521SS</b>								
2007	39,300	42,614,694,756	\$ 1.44	\$ 1,562,548	10.25	11,114,588	\$ 0.03	\$ 29,277
2008	40,676	44,107,519,401	\$ 1.63	\$ 1,766,406	9.51	10,312,169	\$ 0.03	\$ 30,362
2009	42,311	45,879,629,232	\$ 1.48	\$ 1,601,565	10.20	11,060,370	\$ 0.03	\$ 30,362
2010	36,613	40,303,692,335	\$ 1.24	\$ 1,331,563	8.92	9,672,402	\$ 0.03	\$ 30,362
2011	40,253	43,646,329,707	\$ 1.18	\$ 1,279,553	4.88	5,400,963	\$ 0.04	\$ 39,037
2012	42,174	45,731,073,282	\$ 1.09	\$ 1,179,773	8.26	8,995,731	\$ 0.09	\$ 84,338
2013 (partial year)	24,851	35,486,711,498	\$ 0.43	\$ 608,866	2.18	3,112,966	\$ 0.04	\$ 97,119
<b>CO0061ZZ</b>								
2006	87,753	28,687,784,384	\$ 2.50	\$ 817,695	0.00		\$ -	\$ -
2007	91,440	29,872,053,590	\$ 2.28	\$ 746,151	11.53	3,766,690	\$ 0.05	\$ 16,008
2008	80,781	29,330,313,373	\$ 2.06	\$ 674,280	14.25	4,655,276	\$ 0.06	\$ 20,581
2009	89,840	29,294,227,775	\$ 1.86	\$ 543,209	10.93	3,384,266	\$ 0.05	\$ 16,364
2010	90,195	29,495,878,404	\$ 1.68	\$ 546,832	10.38	3,391,001	\$ 0.05	\$ 16,008
2011	94,525	30,879,909,212	\$ 1.79	\$ 583,788	11.79	3,851,628	\$ 0.06	\$ 20,255
2012	94,067	30,730,215,153	\$ 1.79	\$ 583,788	11.06	3,613,147	\$ 0.07	\$ 21,888
<b>CT0013ZZ</b>								
2010	42,271	8,092,611,798	\$ 1.77	\$ 338,475	4.38	838,629	\$ 0.04	\$ 8,041
2011	38,579	7,385,756,655	\$ 1.62	\$ 310,332	3.91	748,550	\$ 0.04	\$ 8,424
2012	37,622	7,202,505,601	\$ 1.34	\$ 265,345	4.59	878,733	\$ 0.05	\$ 10,147
2013 (partial year)	21,946	4,141,660,586	\$ 0.67	\$ 126,651	0.88	168,472	\$ 0.01	\$ 2,686
<b>CT0053ZZ</b>								
2009	59,914	23,465,156,773	\$ 2.84	\$ 1,111,491	4.01	1,570,500	\$ 0.03	\$ 12,141
2010	62,457	24,460,924,561	\$ 3.03	\$ 1,185,512	3.62	1,378,594	\$ 0.03	\$ 11,749
2011	63,936	25,040,106,332	\$ 2.92	\$ 1,142,040	3.51	1,374,677	\$ 0.03	\$ 12,924
2012	57,873	22,865,901,292	\$ 2.42	\$ 945,567	3.64	1,425,591	\$ 0.04	\$ 13,274



2013 (partial year)	23,569	9,230,630,161	\$	0.95	\$	371,672	1.58	618,801	\$	0.02	\$	7,050
<b>CT0009ZZ</b>												
2009	61,567	10,221,583,143	\$	1.85	\$	307,644	9.39	1,588,975	\$	0.16	\$	26,066
2010	58,600	9,729,108,167	\$	1.83	\$	319,598	12.37	2,053,729	\$	0.16	\$	26,564
2011	65,377	10,854,291,136	\$	1.85	\$	306,482	8.27	1,933,027	\$	0.18	\$	29,386
2012	51,167	8,436,039,361	\$	1.61	\$	250,864	5.83	997,926	\$	0.11	\$	17,765
2013 (partial year)	34,861	5,787,797,525	\$	0.67	\$	111,071	1.87	310,467	\$	0.04	\$	6,309
<b>CT0006ZZ</b>												
2009	70,863	12,475,225,166	\$	2.63	\$	463,747	4.88	823,970	\$	0.04	\$	7,042
2010	77,519	13,948,134,332	\$	2.86	\$	503,537	5.93	1,044,048	\$	0.04	\$	7,571
2011	76,343	13,441,175,212	\$	2.72	\$	479,065	4.95	871,507	\$	0.05	\$	8,461
2012	64,313	11,323,010,293	\$	2.61	\$	354,599	3.38	595,000	\$	0.05	\$	8,979
2013 (partial year)	33,256	5,855,096,745	\$	0.76	\$	133,807	2.15	378,533	\$	0.02	\$	4,049
<b>DE0016ZZ</b>												
2009	55,718	11,604,083,122	\$	1.68	\$	348,842	7.83	1,630,707	\$	0.09	\$	18,952
2010	58,066	12,091,039,346	\$	1.57	\$	327,381	8.84	1,799,401	\$	0.11	\$	22,809
2011	48,611	10,123,994,196	\$	1.31	\$	273,242	6.00	1,249,584	\$	0.14	\$	29,573
2012	41,364	8,614,794,145	\$	1.23	\$	255,352	5.40	1,124,626	\$	0.13	\$	26,033
2013 (partial year)	19,662	4,094,788,884	\$	0.48	\$	100,592	1.83	381,123	\$	0.05	\$	10,621
<b>IL0240ZZ</b>												
2009	36,125	1,409,542,256	\$	0.76	\$	29,615	7.09	276,645	\$	0.05	\$	1,834
2010	40,971	1,598,656,814	\$	0.81	\$	31,527	13.05	509,198	\$	0.09	\$	3,590
2011	30,220	1,179,146,766	\$	0.52	\$	20,173	6.86	267,670	\$	0.05	\$	1,990
2012	24,582	935,137,173	\$	0.38	\$	14,927	6.39	249,331	\$	0.05	\$	2,026
2013 (partial year)	15,873	619,362,634	\$	0.17	\$	6,438	1.29	50,335	\$	0.01	\$	429
<b>IL0303ZZ</b>												
2007	63,461	53,273,202,413	\$	1.27	\$	1,086,115	15.89	13,339,035	\$	0.06	\$	50,368
2008	66,173	55,549,980,143	\$	1.49	\$	1,251,636	14.26	11,970,714	\$	0.05	\$	40,294
2009	63,079	52,952,410,787	\$	1.55	\$	1,298,646	13.03	10,938,177	\$	0.06	\$	51,207
2010	62,831	52,744,266,432	\$	1.62	\$	1,357,408	13.26	11,131,252	\$	0.07	\$	58,762
2011	56,063	47,062,601,308	\$	1.59	\$	1,333,064	13.22	11,087,674	\$	0.08	\$	53,726
2012	50,480	42,375,932,518	\$	1.13	\$	947,751	12.14	10,191,057	\$	0.07	\$	59,602
2013 (partial year)	22,988	19,046,010,183	\$	0.41	\$	359,962	3.40	2,864,167	\$	0.02	\$	17,629
<b>IN0009ZZ</b>												
2007	49,233	6,694,286,361	\$	0.68	\$	92,869	2.94	399,758	\$	0.09	\$	12,373
2008	47,210	6,419,202,767	\$	0.70	\$	95,724	4.32	587,399	\$	0.10	\$	13,733
2009	47,432	6,449,373,594	\$	0.76	\$	102,659	3.55	482,701	\$	0.10	\$	14,141
2010	43,563	5,923,414,862	\$	0.58	\$	78,864	4.32	587,399	\$	0.11	\$	14,927
2011	47,871	6,509,115,612	\$	0.69	\$	93,413	3.69	501,737	\$	0.12	\$	15,969
2012	37,790	5,136,391,880	\$	0.62	\$	83,895	3.28	443,269	\$	0.12	\$	16,568
2013 (partial year)	20,115	2,735,933,269	\$	0.28	\$	36,344	0.55	74,785	\$	0.05	\$	6,799
<b>IN0300ZZ</b>												
2007	82,814	26,046,724,290	\$	1.35	\$	423,657	16.55	5,205,289	\$	0.01	\$	3,145
2008	78,760	24,771,497,569	\$	1.42	\$	447,246	12.79	4,022,898	\$	0.01	\$	2,516
2009	68,859	21,657,479,547	\$	1.18	\$	372,076	9.82	3,088,577	\$	0.01	\$	2,202

2010	56,708	17,635,861,840	\$	0.99	\$	311,688	16.73	3,374,785	\$	6.01	\$	2,516
2011	55,019	17,304,410,779	\$	1.07	\$	336,221	6.64	2,098,406	\$	0.01	\$	4,403
2012	46,721	14,694,764,861	\$	1.03	\$	322,362	9.66	3,101,157	\$	0.02	\$	7,234
2013 (partial year)	25,898	8,144,862,654	\$	0.45	\$	141,534	1.86	985,005	\$	0.01	\$	2,202
<b>MA0131ZZ</b>												
2009	67,517	70,612,034,345	\$	2.35	\$	2,460,847	9.40	9,830,840	\$	0.16	\$	184,186
2010	70,349	73,573,281,941	\$	2.59	\$	2,707,664	10.54	11,023,060	\$	0.18	\$	190,342
2011	76,139	79,628,068,676	\$	2.76	\$	2,885,456	10.65	11,138,132	\$	0.20	\$	204,983
2012	65,377	68,375,750,872	\$	2.52	\$	2,636,546	9.29	9,715,798	\$	0.17	\$	175,700
2013 (partial year)	35,315	36,933,554,502	\$	1.60	\$	1,675,426	3.32	3,472,169	\$	0.05	\$	56,475
<b>ND0002ZZ</b>												
2009	88,166	3,845,813,570	\$	1.02	\$	44,362	5.22	227,896	\$	0.03	\$	1,439
2010	82,391	3,593,904,580	\$	0.91	\$	39,738	5.77	251,887	\$	0.03	\$	1,178
2011	80,855	3,526,870,803	\$	0.96	\$	41,701	6.02	262,592	\$	0.02	\$	1,003
2012	65,409	2,853,154,102	\$	0.63	\$	35,030	5.31	231,622	\$	0.03	\$	1,309
2013 (partial year)	51,626	2,251,939,642	\$	0.47	\$	20,632	1.66	72,409	\$	0.01	\$	611
<b>NH0007ZZ</b>												
2010	36,303	6,596,088,096	\$	1.06	\$	192,416	2.52	457,874	\$	0.03	\$	5,451
2011	33,194	6,031,276,964	\$	0.95	\$	172,975	2.40	436,070	\$	0.03	\$	4,542
2012	30,466	5,535,475,841	\$	0.85	\$	153,897	2.88	523,284	\$	0.03	\$	5,087
2013 (partial year)	17,483	3,176,622,055	\$	0.36	\$	65,956	0.69	125,370	\$	0.01	\$	1,817
<b>NJ0000FB</b>												
2010	43,498	15,543,521,719	\$	1.48	\$	527,077	6.72	2,401,325	\$	0.11	\$	40,737
2011	43,667	15,604,044,395	\$	1.31	\$	468,473	5.69	2,104,733	\$	0.11	\$	38,950
2012	36,612	13,083,035,709	\$	1.22	\$	437,364	4.47	1,587,310	\$	0.09	\$	31,603
2013 (partial year)	17,269	6,176,162,032	\$	0.46	\$	172,595	1.68	960,331	\$	0.03	\$	11,453
<b>OH0033ZZ</b>												
2010	93,253	22,881,196,596	\$	1.96	\$	481,657	2.16	529,995	\$	0.02	\$	5,889
2011	101,442	24,890,502,879	\$	2.16	\$	530,486	2.95	650,225	\$	0.03	\$	7,852
2012	67,641	16,596,892,722	\$	1.63	\$	400,931	3.14	770,456	\$	0.04	\$	10,305
2013 (partial year)	33,343	6,181,364,112	\$	0.99	\$	242,178	0.60	196,264	\$	0.01	\$	3,190
<b>OR0052ZZ</b>												
2010	53,082	31,408,201,171	\$	0.92	\$	546,129	4.10	2,425,925	\$	0.05	\$	31,951
2011	56,192	34,431,530,787	\$	0.98	\$	578,080	3.81	2,254,335	\$	0.05	\$	31,951
2012	47,579	28,151,846,678	\$	0.84	\$	495,835	3.91	2,313,504	\$	0.06	\$	35,501
2013 (partial year)	25,603	15,149,048,968	\$	0.42	\$	250,876	1.31	775,113	\$	0.03	\$	15,384
<b>OR0053ZZ</b>												
2010	37,252	11,484,555,242	\$	0.64	\$	197,307	7.18	2,213,537	\$	0.06	\$	17,881
2011	36,616	11,266,318,136	\$	0.62	\$	191,449	6.16	1,899,079	\$	0.05	\$	16,339
2012	33,987	10,478,012,892	\$	0.62	\$	190,833	6.07	1,871,332	\$	0.05	\$	17,264
2013 (partial year)	15,764	4,865,133,336	\$	0.27	\$	83,239	1.53	471,687	\$	0.02	\$	6,782
<b>PA0143ZZ</b>												
2010	43,305	17,549,592,262	\$	1.42	\$	574,218	7.38	2,990,634	\$	0.07	\$	27,961
2011	45,841	18,576,247,960	\$	1.42	\$	575,028	6.54	2,690,760	\$	0.07	\$	29,987
2012	40,895	16,572,095,325	\$	1.24	\$	502,897	5.90	2,390,887	\$	0.07	\$	27,151

2013 (partial year)	21,114	8,556,985,319	\$	0.60	\$	244,357	0.93	376,668	\$	0.06	\$	25,530
<b>PA0183ZZ</b>												
2010	57,343	48,187,875,945	\$	1.62	\$	1,363,033	6.21	5,218,518	\$	0.07	\$	62,185
2011	55,921	46,992,867,044	\$	1.52	\$	1,275,638	5.91	4,965,415	\$	0.08	\$	63,028
2012	44,923	37,750,487,482	\$	1.16	\$	972,275	5.50	4,621,876	\$	0.07	\$	61,345
2013 (partial year)	24,483	20,657,825,480	\$	0.54	\$	636,138	1.36	1,142,864	\$	0.03	\$	21,009
<b>PA0233ZZ</b>												
2010	64,295	50,562,273,035	\$	1.62	\$	1,276,347	5.10	4,010,701	\$	0.08	\$	66,059
2011	63,512	49,946,756,226	\$	1.76	\$	1,393,299	7.36	5,767,892	\$	0.11	\$	82,573
2012	51,708	40,664,059,076	\$	1.25	\$	983,015	6.88	5,410,515	\$	0.11	\$	84,146
2013 (partial year)	25,863	20,339,075,790	\$	0.65	\$	514,313	2.95	1,612,145	\$	0.04	\$	29,097
<b>TN0012ZZ</b>												
2009	51,125	8,229,634,326	\$									
2010	48,781	7,852,305,425	\$	1.09	\$	176,102	8.48	1,365,034	\$	0.04	\$	6,600
2011	48,761	7,852,305,425	\$	0.96	\$	154,049	11.54	1,857,605	\$	0.05	\$	8,049
2012	49,393	7,950,916,259	\$	1.05	\$	169,663	7.08	1,139,675	\$	0.04	\$	6,439
2013 (partial year)	46,686	7,488,776,064	\$	1.03	\$	166,283	7.17	1,541,162	\$	0.04	\$	7,083
2010	24,510	3,945,423,356	\$	0.49	\$	78,715	2.74	441,061	\$	0.02	\$	3,219
<b>TN0078ZZ</b>												
2004	44,186	7,630,194,502	\$	0.79	\$	136,938	n/a	n/a	\$	n/a	\$	n/a
2005	46,757	8,074,242,774	\$	0.81	\$	139,356	n/a	n/a	\$	n/a	\$	n/a
2006	48,014	8,291,291,020	\$	0.97	\$	166,813	n/a	n/a	\$	n/a	\$	n/a
2007	49,454	8,539,852,370	\$	0.95	\$	163,877	12.95	2,236,256	\$	0.13	\$	21,753
2008	48,766	8,421,192,559	\$	1.05	\$	181,491	13.03	2,250,073	\$	0.12	\$	20,895
2009	49,727	8,587,121,161	\$	1.18	\$	203,249	11.08	1,909,885	\$	0.10	\$	17,268
2010	53,533	9,244,278,757	\$	1.14	\$	197,550	15.26	2,635,158	\$	0.10	\$	17,441
<b>WA0035ZZ</b>												
2010	55,808	11,050,197,332	\$	1.33	\$	263,741	26.50	5,247,106	\$	0.46	\$	91,280
2011	42,498	8,414,692,810	\$	1.01	\$	200,578	5.92	1,172,184	\$	0.12	\$	23,562
2012	39,482	7,817,524,827	\$	0.91	\$	179,788	5.23	1,035,561	\$	0.12	\$	22,968
2013 (partial year)	17,023	3,370,641,892	\$	0.43	\$	85,934	1.12	221,764	\$	0.03	\$	5,544
<b>WA0036ZZ</b>												
2010	24,271	7,421,300,882	\$	0.54	\$	164,810	2.94	888,984	\$	0.05	\$	15,289
2011	24,577	7,514,970,444	\$	0.56	\$	172,454	3.21	981,522	\$	0.06	\$	18,346
2012	23,205	7,095,490,696	\$	0.55	\$	167,256	2.83	865,329	\$	0.07	\$	19,875
2013 (partial year)	11,332	3,464,965,640	\$	0.28	\$	85,310	1.03	314,943	\$	0.03	\$	8,256
<b>WA0102ZZ</b>												
2010	59,914	40,726,753,966	\$	0.96	\$	649,845	6.09	4,139,702	\$	0.11	\$	74,093
2011	53,186	38,153,450,624	\$	0.82	\$	626,733	4.80	3,282,818	\$	0.09	\$	63,897
2012	53,971	36,687,037,127	\$	0.89	\$	607,700	5.26	3,575,506	\$	0.11	\$	74,773
2013 (partial year)	24,339	18,674,623,927	\$	0.44	\$	300,451	1.44	378,046	\$	0.03	\$	20,393
<b>WA0811KA</b>												
2010	88,590	10,346,724,572	\$	1.78	\$	207,892	31.63	3,694,163	\$	0.49	\$	57,112
2011	90,164	10,530,480,839	\$	1.76	\$	205,089	29.76	3,475,790	\$	0.65	\$	76,266
2012	75,655	8,836,052,666	\$	1.58	\$	184,269	19.97	2,332,356	\$	0.52	\$	60,849
2013 (partial year)	37,972	4,434,595,177	\$	0.70	\$	81,171	8.67	779,009	\$	0.20	\$	22,891

[illegible]

Note: The data in this table pertains to the subset of 31 existing buildings that have achieved either a Green Globes or LEED certification, not the ENERGY STAR labeled buildings. Highlighted row for each building indicates the year in which the building received LEED or Green Globes certification.

## Attachment C

## Active Capital New Construction Projects

Region	Project Name	New Construction Appropriation (4/15/13)	New Construction Obligations (4/15/13)	Estimated Total Project Cost
01	VT, Derby Line, Border Station	\$ 36,329,000	\$ 2,540,474	\$ 21,544,000
01	ME, Van Buren U.S. Land Port of Entry	\$ 45,127,000	\$ 44,812,980	\$ 45,127,000
01	ME-Calais-Milltown LPOE New	\$ 64,899,477	\$ 64,899,477	\$ 64,899,477
02	NY, Brooklyn, United States Courthouse Annex—GPO	\$ 536,284,000	\$ 536,182,586	\$ 536,284,000
02	PR, San Juan FBI Field Office Consolidation	\$ 35,934,980	\$ 35,749,153	\$ 130,713,980
03	Norfolk, VA, U.S. Courthouse Annex	\$ 19,809,000	\$ 17,497,560	\$ 133,620,000
03	PA, Harrisburg, Harrisburg Courthouse	\$ 26,000,000	\$ 13,698,212	\$ 179,000,000
04	AL, Anniston, U.S. Courthouse	\$ 4,400,000	\$ 141,622	\$ 42,930,000
04	SC, Greenville, Carroll A. Campbell Jr. U.S. Courthouse	\$ 11,000,000	\$ 6,014,695	\$ 98,100,000
04	GA, Savannah, U.S. Courthouse Annex	\$ 12,697,000	\$ 4,656,589	\$ 100,000,000
04	AL, Mobile, U.S. Courthouse	\$ 61,290,000	\$ 12,253,251	\$ 102,290,000
04	TN, Nashville, U.S. Courthouse / Nashville, TN	\$ 26,095,000	\$ 24,749,277	\$ 180,760,000
04	NC, Charlotte Federal Courthouse	\$ 8,500,000	\$ 171,663	\$ 193,260,000
04	FL, Tampa Sam M. Gibbons U.S. Courthouse	\$ 69,487,426	\$ 68,987,426	\$ 69,487,426
04	FL, Miami, FBI Building	\$ 190,947,353	\$ 161,464,531	\$ 190,675,000
05	OH, Toledo, New Toledo U.S. Courthouse	\$ 6,499,753	\$ 5,165,012	\$ 123,000,000
06	MO, St. Louis, Thomas Eagleton U.S. Courthouse	\$ 250,249,300	\$ 250,232,904	\$ 250,249,300
07	TX, San Antonio, San Antonio Courthouse	\$ 12,000,000	\$ 7,023,573	\$ 129,420,000
07	TX, Austin U.S. Courthouse	\$ 114,632,500	\$ 113,854,277	\$ 114,632,500
07	AR, Little Rock, United States Courthouse Annex	\$ 7,170,316	\$ 7,170,316	\$ 7,170,316
07	TX, El Paso, Tornillo-Guadalupe Land Port of Entry	\$ 95,855,000	\$ 60,402,640	\$ 79,600,000
07	NM, Santa Teresa USBS Santa Teresa Admin Bldg	\$ 10,000,000	\$ 9,813,397	\$ 11,305,000
08	UT, Salt Lake City, Frank E. Moss U.S. Courthouse Annex	\$ 226,364,000	\$ 221,505,221	\$ 226,364,000
08	ND, Portal, Border Station	\$ 43,680,000	\$ 42,365,910	\$ 43,700,000
08	CO, Lakewood, Denver Federal Center Remediation	\$ 39,033,000	\$ 27,529,047	\$ 45,340,000
09	AZ, Yuma U.S. Courthouse	\$ 25,537,863	\$ 25,537,353	\$ 26,261,553
09	AZ, San Luis, Land Port of Entry I	\$ 7,053,000	\$ 1,301,357	\$ 82,000,000
09	CA, Calexico, Calexico West Border Station	\$ 23,787,000	\$ 16,775,051	\$ 352,000,000
09	CA, San Ysidro, Land Port of Entry	\$ 298,343,253	\$ 248,958,880	\$ 726,000,000
09	AZ, Nogales West US Land Port of Entry	\$ 173,835,236	\$ 172,969,240	\$ 261,000,000
11	DC, Washington, Department of Transportation	\$ 42,000,000	\$ 39,866,944	\$ 42,000,000
11	DC, Washington, Southeast Federal Center Site Remediation	\$ 75,856,500	\$ 58,858,954	\$ 75,856,500
11	MD-White Oak-FDA	\$ 1,189,289,000	\$ 1,169,900,406	\$ 1,189,289,000
11	DC, Washington DHS Consolidation and Development of St. Elizabeths Campus	\$ 910,298,000	\$ 900,366,484	\$ 2,646,277,000



WEDNESDAY, APRIL 10, 2013.

**SMALL BUSINESS ADMINISTRATION**

**WITNESS**

**PEGGY GUSTAFSON, INSPECTOR GENERAL, SMALL BUSINESS ADMINISTRATION**

Mr. CRENSHAW. Well, welcome, Mr. Serrano, and welcome you all. Good morning. We will call this meeting to order. Today it is April 10th, Wednesday. And today we finally received the president's 2014 budget request. It was due on February the 4th, but it is better late than never. Those of us on this committee are ready to move forward and keep doing our work.

Mr. SERRANO. It is a work in progress.

Mr. CRENSHAW. That is right. So today we have with us Peggy Gustafson. She is the Inspector General for the Small Business Administration. She has been there since 2009; has a budget of \$16.3 million in fiscal year 2012. The SBA Office of Inspector General has a significant job in conducting oversight of the SBA's diverse portfolio of programs, ensuring that the taxpayers in the small business interest are protected and served well.

The SBA plays a critical role in maintaining and strengthening our nation's economy, assisting small businesses, providing small businesses with access to capital, opportunities to compete for government contracts, and other technical assistance. Additionally, the SBA helps businesses and homeowners affected by disasters get back on their feet through the Disaster Loan Program. And this year, SBA was appropriated \$800 million to provide relief and recovery to small businesses, homeowners, and renters affected by Hurricane Sandy. This is a massive effort that needs strong oversight.

And while the SBA's programs are vital to getting our economy back on track, the agency has to confront significant challenges in executing its mission. Fraud continues to be a problem, affecting all of SBA programs. Default rates within the business loan program remain high, costing the government and taxpayers millions of dollars. Excessive improper payments, weaknesses in procurement procedures, and poor lender oversight are all issues that the SBA must address.

The Office of Inspector General was created to promote economy, efficiency and effectiveness in SBA programs and operations and to deter and detect waste and abuse. So your job is an important one. We look forward to hearing your testimony and like now to recognize the ranking member of the Subcommittee for any opening statement he might make.

Mr. SERRANO. Thank you, Mr. Chairman. I would also like to join you in welcoming the Inspector General of Small Business Admin-

istration to the hearing today. The SBA, as the chairman said, plays a vital role in all of our districts, helping businesses to get started, to expand, and to serve and employ our constituents. And your office plays an important role in making sure that the assistance is provided as effectively with as little waste as possible.

I will be interested in hearing whether you are starting to see an increased level of fraud and what challenges you are facing, trying to address these problems while coping with funding at last year's level. In addition, I look forward to hearing about both how the sequester will affect your ability to fulfill your responsibilities and how the impact of the sequester on the agency as a whole will affect your work.

Lastly, I am interested in hearing your observations about the SBA's role in helping New Yorkers recover from Hurricane Sandy. Now I cannot emphasize enough that that has been, as you well know, something that we New Yorkers thought would never happen in our part of the world, and the devastation has been massive. And you play a vital role, the SBA does. And we would like to know what you know, what you see, and what adjustments have to be made, if any. Thank you so much. Thank you, Mr. Chairman.

Mr. CRENSHAW. Thank you. And now Ms. Gustafson, we will turn to you. And if you will make some opening remarks in the five-minute range, and we will submit your written testimony for the record. So please proceed.

Ms. GUSTAFSON. Thank you very much. And thank you, Chairman Crenshaw and Ranking Member Serrano, for asking me to come testify before your Subcommittee today. I am extremely proud to be here and represent the dedicated men and women of the Office of Inspector General in the SBA. As you know, my office is an independent office within the agency. We conduct and supervise audits, inspections, and investigations related to SBA programs and supporting operations. Our job is to detect and prevent waste, fraud, and abuse and promote economy efficiency and effectiveness in the administration management of all the programs of the Small Business Administration.

I believe that our investigations and report recommendations are having a very positive impact on the integrity of SBA programs, and that the results are very measurable. During fiscal year 2012, my office issued 22 reports containing 126 recommendations for improving SBA operations, reducing fraud and unnecessary losses, and recovering funds. In addition, The Office of Inspector General criminal investigations led to 59 indictments and 59 convictions of subjects who had defrauded the government. In all, the efforts of my office resulted in more than \$90 million in office-wide dollar accomplishments during fiscal year 2012. Our fiscal year 2012 operating budget was \$17.3 million, which included a \$1 million transfer from the Disaster Fund, specifically for our work in the disaster area, so that the total office-wide dollar accomplishments represented more than fivefold return on investment to the taxpayers through the Office of Inspector General.

Now, though, these figures confirm that our work is focused on the areas of high risk, I am concerned about the continued financial and operational risks that exist within the agency. For example, in the loan programs, the 7A and 504 loan programs, the max-



imum allowable guarantee for loan has grown from \$2 million per loan to \$5 million; for manufacturers in the 504 loan program it is \$5.5 million, which, of course, has the effect of expanding the potential exposure of the taxpayer, should these loans eventually default. So this exposure, combined with a swollen portfolio and the limited agency oversight, does increase the possibility of future losses. SBA's payments of guarantees on defaulted loans had evidenced an increase from the baseline of 2007, when \$1 billion was paid in guarantees on defaulted loans to \$5 billion in 2010, \$3.4 billion in 2011, and \$2.6 billion in 2012. Now, it is noticeable and noted that these figures are going the right direction. But, again, we are concerned, especially given the larger loan amounts that are now allowable under the programs.

The SBA contracting programs continue to be subject to fraud and weak federal oversight, and the shortcomings in the agency's IT systems might hinder SBA's ability to effectively manage the programs. I do appreciate the opportunity to discuss how we have proposed to address the noted and persistent risk this fiscal year, though the budget is not out quite yet. So in the president's fiscal 2013 budget, the president had requested a \$3.1 million increase in our budget, and we had received a mark in the House of \$18.267 million, including the disaster transfer. And in the Senate, the mark was matched at the president's request of \$20.4 million. And, of course, we ended up operating under a CR, which we will do for the remainder of the year.

But I am poised to use additional resources, should I ever get them, to effectively target early defaulted loans, fraud, and lender negligence, and to increase the capacity of our existing investigative personnel. I will speed it up.

Mr. CRENSHAW. No, no, take your time.

Ms. GUSTAFSON. Thank you. I do talk fast. The additional resources that we have requested in the budget justifications, including the budget justifications in the past, included resources to establish a dedicated early defaulted loan review group to identify problem loans, to enhance my investigative capacity, and to enhance the operations of the Office of Inspector General hotline. When lender negligence is found, the early defaulted loan review group would recommend non-payment of the guarantee or recovery if the guarantee is already paid; would help target the most offending lenders to obtain corrective actions; and I think, perhaps most importantly, identify trends for operational improvement by SBA if there are weaknesses in the actual process. This group would help identify those trends and fix it before the loans go out. When suspected fraud is identified, the loans will be investigated.

Over the past decade, we have obtained convictions and guilty pleas on numerous cases involving loan agent fraud and SBA-guaranteed loans, totaling excesses \$358 million. The Office of Inspector General handles an average of 250 criminal and civil fraud investigations per year, and annually obtains multiple indictments and convictions of recoveries in the area of tens of millions of dollars. However, resource constraints do sometime preclude us from initiating or continuing a number of investigations. For example, over the last three years, the OIG has administratively closed 171 allegations with potential losses estimated at over \$136 million, which

may have met prosecutorial thresholds but could not be further investigated due to a lack of resources. Also, over the last three years, the office has proactively identified over 574 suspect loans with values estimated at over \$503 million that contained characteristics typical of problem loans. But, again, due to the limited resources, these loans could not be further reviewed to identify lender deficiencies or indications of fraud.

Additional investigative support personnel would enhance the existing investigative capacity and allow more effective utilization of existing investigative resources in a cost-effective manner. For example, we estimate payroll costs for an investigative analyst to be only 67.5 percent to that of a criminal investigator, an actual 1811 investigator. With the support of the Subcommittee, we could increase both the effectiveness and the efficiency of these investigations.

Regarding our hotline operation, during fiscal year 2012, the hotline received 535 complaints, which were processed by one professional staff member. Additional staff resources are required to adequately analyze incoming complaints for possible referral for investigation or other resolution. This is especially crucial because this is often the only time the public has contact with my office. If you think you know of waste, fraud, or abuse, what you do is you call the hotline. Or if you think you are a whistleblower that is being retaliated against, that is the hotline. And so it is very difficult to have an effective hotline with one person. Now, I have two; I have actually dedicated resources within my constraints to have two, but it is difficult. And given the fact that we work for the public, that becomes problematic, or at least it could be a lot better.

In short, much work has been done, but much work remains to be done. Additional resources would undoubtedly net a significant return on investment to the taxpayer and a better SBA. So I thank you very much for the opportunity to speak with you, and I look forward to your questions.

[The information follows:]



**STATEMENT OF**

**PEGGY E. GUSTAFSON  
INSPECTOR GENERAL  
U.S. SMALL BUSINESS ADMINISTRATION**

**BEFORE THE**

**COMMITTEE ON APPROPRIATIONS  
SUBCOMMITTEE ON FINANCIAL SERVICES AND  
GENERAL GOVERNMENT  
U.S. HOUSE OF REPRESENTATIVES**

**APRIL 10, 2013**

**PEGGY E. GUSTAFSON**  
**INSPECTOR GENERAL**  
**U.S. SMALL BUSINESS ADMINISTRATION**

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**INTRODUCTION**

Chairman Crenshaw, Ranking Member Serrano, and distinguished members of the Subcommittee, thank you for giving the Small Business Administration (SBA or Agency) Office of Inspector General (OIG) an opportunity to discuss our oversight activities of SBA programs and operations.

The OIG was established within SBA by statute to promote economy, efficiency, and effectiveness and to deter and detect waste, fraud, and abuse in the Agency's programs and operations. Every year, our staff of approximately 104 employees—which includes criminal investigators, auditors and program analysts, attorneys, and support staff—conduct criminal investigations, audits, and other reviews, resulting in numerous indictments, convictions, and monetary payments of fraud perpetrators and many recommendations to the Agency for improvement and elimination of wasteful or inefficient practices.

During Fiscal Year (FY) 2012, the SBA OIG operated at an enacted budget level of \$17.3 million, which included a \$1.0 million transfer from the SBA Disaster Loan Program Account. Approximately 84 percent of our expenditures are attributed to payroll expenses for our 104<sup>1</sup> employees. The OIG issued 22 reports containing 126 recommendations for improving SBA operations, reducing fraud and unnecessary losses, and recovering funds in FY 2012. In addition, OIG investigators obtained 59 indictments and 59 convictions of subjects who defrauded the government. In all, OIG efforts resulted in more than \$90 million in office-wide dollar accomplishments during FY 2012.

**OVERSIGHT PRIORITIES**

The SBA was established to maintain and strengthen the nation's economy by protecting the interests of and assisting small businesses, and by helping families and businesses recover from disasters. While SBA's programs are essential to strengthening America's economy, the Agency faces a number of challenges in carrying out its mission, including fraudulent schemes affecting all SBA programs, significant losses from defaulted loans, procurement flaws that allow large firms to obtain small business awards, excessive improper payments, and outdated legacy information systems. The Agency also faces significant management challenges.

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<sup>1</sup> Includes positions funded from supplemental appropriations—the American Recovery and Reinvestment Act of 2009 and the Consolidated Security, Disaster Assistance, and Continuing Appropriations Act of 2009.

In accordance with the Reports Consolidation Act of 2000, the OIG released its *Report on the Most Serious Management and Performance Challenges Facing the Small Business Administration in FY 2013* in October 2012. This report represents our current assessment of Agency programs and/or activities that pose significant risks, including those that are particularly vulnerable to fraud, waste, error, mismanagement, or inefficiencies. Our report is based on specific OIG, Government Accountability Office (GAO), and other official reports, as well as our general knowledge of SBA's programs and operations.

**Summary of the Most Serious Management and Performance Challenges Facing the SBA in FY 2013**

	Challenge	Color Scores					
		Status at End of FY 2012				Change from Prior Year	
		Green	Yellow	Orange	Red	Up ↑	Down ↓
1	Small Business Contracting	1		2		1	
2	IT Security		3	2			
3	Human Capital		1	3		1	
4	Loan Guaranty Purchase		1				
5	Lender Oversight	1	1	1		1	
6	8(a) Business Development Program		1	1	1		
7	Loan Agent Fraud	1	1			1	
8	Loan Management and Accounting System		1		3	1	3
9	Improper Payments – 7(a) program		2	2		1	
10	Improper Payments – Disaster Loan program		1				
11	Acquisition Management (NEW)						
	<b>TOTAL</b>	<b>3</b>	<b>12</b>	<b>11</b>	<b>4</b>	<b>6</b>	<b>3</b>

Overall, in FY 2012, the Agency made improvements across all the challenges, with the exception of one of the recommended actions under Management Challenge #6 and three of the recommended actions under Management Challenge #8. Specifically, Management Challenge #6—The Section 8(a) Business Development program needs to be modified so more firms receive business development assistance, standards for determine economic disadvantage are justifiable, and the SBA ensures that firms follow 8(a) regulations when completing contracts—remains at a rating of Red or no progress. Management Challenge #8—SBA needs to modernize its Loan Accounting System and migrate it off the mainframe—was downgraded from a rating of Orange, or limited progress, to a rating of Red, or no progress.

Despite these two Management challenges, the progress on all other Management Challenges was notable. The effort made by Agency staff and leadership throughout FY 2012 on the recommended actions demonstrated commitment to improving the Agency's programs and operations. The Agency's efforts are reflected in the overall elevation of Management Challenge ratings.

Pursuant to P.L. 113-2, the OIG was appropriated \$5 million to provide effective oversight of the SBA's disaster response to Hurricane Sandy. This funding level is based on experience with major disasters in the past, such as the Gulf Coast Hurricanes in 2005. The supplemental funding will be used to support approximately 5 auditors and 5 criminal investigators and associated operating costs for a period of at least 4 to 6 years. Availability of funds for this timeframe is particularly important because many times fraudulent loans are not immediately identified, have a deferment period for repayment, and take years to default. There is a five-year statute of limitations (from the date of the last false statement) to prove a false statement to the SBA.

### **PLANNED ACTIVITIES**

In addition to conducting audits and reviews that are required by statutes and other directives, the OIG plans to focus on the most critical risks facing the SBA. Several areas of emphasis are discussed below.

#### *Financial Assistance*

Over the last several years, losses in the SBA's loan programs have increased substantially. Some of the increase in SBA losses correlates to similar root causes seen in the mortgage industry, such as limited oversight of lenders and loan agents, poor lender loan processing, unscrupulous borrowers, and complicit brokers and lenders. The SBA also faces a heightened risk of losses and improper payments due to expedited loan processing initiatives and its considerable reliance on outside financial institutions over which the Agency does not always exercise adequate oversight.

The Agency's business loan programs include: (1) the Section 7(a) program, in which the SBA guarantees lender-originated loans to small businesses made by lenders; and (2) the Section 504 program, in which the SBA guarantees repayment of debentures that are sold by Certified Development Companies (CDCs) to investors to create funds for loans to small businesses. The majority of loans made under the 7(a) program are made with little or no review by the SBA prior to loan approval because the Agency has delegated most of the credit decisions to the lenders originating these loans.

Two recent developments in SBA's 7(a) loan guaranty program highlight the need for continued vigilance in the OIG's oversight of the Agency. First, SBA's

payments of guaranties on defaulted loans are significantly higher than a baseline of FY 2007—from \$1 billion in FY 2007 to \$5 billion in FY 2010, \$3.4 billion in FY 2011, and \$2.6 billion in FY 2012—however, it is noted these figures are moving in the right direction. Although some defaults are likely due, in part, to economic conditions, many OIG audits and investigations of loans that have defaulted early have identified problems with the loan origination, including lender negligence and fraud. Second, as a result of statutory changes in 2010, the size of loans that SBA guarantees more than doubled from \$2 million to \$5 million, thus dramatically expanding the potential exposure to the taxpayer. This exposure, combined with a swollen portfolio and limited Agency oversight, increase the possibility of future losses.

The OIG is using its resources to more effectively address the growing financial losses in SBA lending due to lender errors and various fraud schemes. The OIG is utilizing an Early Defaulted Loan Working Group to perform in-depth analyses of loans that default within 18 months of final disbursement. From this, the OIG either makes recommendations for loan guaranty recoveries, or if fraud is apparent, conducts criminal investigations to refer suspected fraud for prosecution. The OIG also assesses trends of lending problems. Despite past successes, such activities have been limited due to resource constraints.

The OIG's national initiative to detect fraud committed by loan agents, such as packagers and brokers, continues to be a priority for the office. A loan agent is sometimes hired by an applicant or lender to assist the applicant in obtaining an SBA loan. Although honest loan agents help small businesses gain access to capital, some dishonest ones have perpetrated fraudulent schemes involving tens of millions of dollars in loans. These fraudulent loans often default for non-payment, and the SBA is forced to use taxpayer funds to purchase the guaranteed portions of the loans. In a recent case, an OIG investigation led to the indictment of three loan brokers and their company for conspiring to provide false information to SBA in order to obtain SBA loans. This is a complex loan fraud scheme involving loans valued at approximately \$100 million. Over the past decade, the OIG has obtained convictions and guilty pleas on numerous cases involving loan agent fraud on SBA-guaranteed loans, totaling in excess of \$358 million.

The OIG recently has initiated a review of the examination process for the Small Business Investment Company (SBIC) program. In addition, the OIG will continue to conduct audits of business loans that default quickly because past work has shown such loans were not always properly originated and that effective controls and procedures were not in place to prevent improper payments. Future OIG efforts will focus on: (1) SBA's loan origination process to determine its compliance and effectiveness; (2) SBA quality control programs to determine the extent to which programs are mitigating the risk of loss; (3) SBA's management of certain loan programs; and (4) the reliability of data in the Agency's Loan Accounting System.

OIG audits related to disaster loans will continue to focus on loan origination, disbursement, repayment, servicing, and liquidation activities. Such audits may assess whether the SBA processed homeowner and business loan applications in accordance with the Agency's procedures, verified uses of loan proceeds before loans were fully disbursed, and appropriately identified duplicate benefits. Future efforts will focus on the loss verification process and analyzing, through cross cutting projects, whether there are redundancies among agencies providing various forms of assistance to disaster victims. Such efforts would focus on determining whether there is potential to reduce costs across agencies while streamlining and consolidating processes for disaster victims. The OIG also will continue to investigate allegations of unauthorized use of loan proceeds; overstatement of financial losses; material false statements in the application process; false/counterfeit supporting documentation; and false assertions regarding primary residency in affected areas at the times of the disasters. As of September 30, 2012, the OIG had 26 open cases involving disaster loans with potential dollar losses of over \$12.8 million.

In response to the increase in fraud following Hurricanes Katrina, Wilma, and Rita, the OIG and other law enforcement organizations established the National Center for Disaster Fraud. From FY 2006 through FY 2012, the OIG, in conjunction with other law enforcement agencies, has produced 86 arrests, 95 indictments, and 91 convictions related to wrongdoing in SBA's Disaster Loan program for these three hurricanes. Investigations for these disasters—to date—have resulted in over \$6.6 million in court-ordered restitution and related recoveries, as well as the denial of nearly \$4.5 million in loans to potentially fraudulent borrowers. In addition, the OIG has investigated fraud related to 2008 Hurricanes Ike and Gustav.

### *Government Contracting and Business Development*

The SBA directs significant efforts toward helping small businesses obtain Federal contracts and providing other business development assistance. The SBA's Office of Government Contracting and Business Development is tasked with helping small businesses obtain a fair proportion of Federal contracting opportunities and helping small, disadvantaged, and women-owned businesses build their potential to compete more successfully in a global economy. Oversight of the Government Contracting and Business Development programs, including investigating allegations that ineligible companies are fraudulently benefitting from these programs, remains a key priority for the OIG. As of September 30, 2012, the OIG had 62 open government contracting cases, with potential dollar losses of over \$1.5 billion based on the total dollar value of the contracts.

The OIG has in the past year received a significant increase in the number of qui tam False Claims Act suits that have been filed by private sector parties alleging



fraud in SBA government contracting programs. In light of increases in qui tam claims that the government has experienced over the past several years, the OIG expects the volume of this work to increase. This will require expenditure of additional resources to investigate these allegations.

Aside from these issues, there are other reasons to be concerned about government contracting programs.

- There has been a high level of congressional interest in small businesses receiving a fair share of Federal contracts. The OIG will continue to assess whether the SBA is taking adequate steps to ensure the integrity of small business contracting, with an emphasis on issues such as the accuracy of reporting small business contract activity, large businesses being classified as small businesses, adherence to regulations to protect small businesses, training of government contracting personnel, deterring fraudulent acquisition of government contracts, and bundling of contracts.
- The Section 8(a) Business Development program continues to be susceptible to major vulnerabilities. These include limited program oversight; inequitable distribution of contracting opportunities among participants; a lack of reasonable, measurable, consistent, and mandatory criteria pertaining to economic disadvantage; a lack of implemented criteria defining business success for purposes of program graduation; and misrepresentation by companies as small, minority-owned, or disadvantaged businesses to gain an unfair advantage in the Federal marketplace. The OIG will continue to review these issues and the SBA's management of the Section 8(a) program.
- The Historically Underutilized Business Zone (HUBZone) program provides Federal contracting assistance to small businesses located in economically distressed areas with the intent of stimulating economic development. The Service-Disabled Veteran-Owned Small Business (SDVOSB) program provides more opportunities in Federal contracting for disabled veterans who own small businesses. The GAO has identified significant control weaknesses in these programs that have allowed ineligible firms to receive millions of dollars in contracts. The OIG will examine the SBA's claim that it has implemented a more rigorous HUBZone certification process in the hopes of preventing ineligible firms from achieving certification. In addition, the OIG plans to review the HUBZone decertification process once the SBA completes its reengineering of this process. The OIG also will continue to pursue prosecution, civil fraud recovery, and debarment of contractors who improperly obtain HUBZone, SDVOSB, and other preferential contracts.

### *Financial Management and Information Technology*

The OIG will continue to oversee the audits of the SBA's financial statements, as well as Federal Information Security Management Act (FISMA) and Federal Information Systems Controls Audit Manual (FISCAM) reviews, which are conducted by an Independent Public Accountant under a contract with the OIG. The OIG also will continue its review of the SBA's compliance with the Improper Payments Elimination and Recovery Act (IPERA). The OIG anticipates that the scope of financial statement audits will continue to expand as a result of growing direct and guaranteed loan portfolios. The OIG plans to review SBA's actions to implement the requirements of the GPRA Modernization Act of 2010. The review will survey the sources and use of performance information in program decision-making and evaluate the effectiveness of corrective actions deployed to address long standing challenges, needs, and problems.

The OIG also will continue to monitor systems development activities related to improvements to the SBA's Loan Management and Accounting System, a system that is critical to SBA's ability to administer its loan portfolio, which in FY 2012 totaled over \$102 billion. OIG efforts will include determining whether adequate System Development Lifecycle Controls are in place as the SBA endeavors to move its batch COBOL systems from the mainframe to a new hosting environment. As threats to disrupt cyber-based systems continue to escalate, the Agency must take steps to improve controls to prevent outages and loss of sensitive data and to ensure the continuity of mission critical operating systems. The OIG will conduct audits to assess the security of the SBA's computer operating system, network, and hosted applications by performing assurance reviews. The OIG also will review the sufficiency of SBA resources used to manage computer security, maintain systems, provide technical support, and administer security training.

### *Security Operations*

The OIG's Office of Security Operations (OSO) is responsible for processing name checks and, where appropriate, fingerprint checks to ensure that applicants meet certain character standards before participating in programs involving business loans, disaster assistance loans, Section 8(a) certifications, surety bond guarantees, SBICs, and CDCs. As a result of OIG referrals during FY 2012, SBA business loan program managers declined 54 applications totaling over \$37.2 million, and disaster loan program officials declined 26 applications totaling over \$2.1 million, due to character issues of loan applicants. In addition, the Section 8(a) program declined 31 applications for admission. Over \$300 million in loans have been declined during the last 10 years due to character problems identified by the OIG, thereby making credit and SBA assistance available to otherwise eligible applicants. The OSO also is responsible for performing required background investigations for covered SBA employees and adjudicate SBA employees/contractors for issuance of PIV cards pursuant to HSPD-12

background investigation requirements. During FY 2012, the OIG initiated 333 background investigations and issued 49 security clearances for SBA employees and contractors.

### *Review of Proposed Regulations and Initiatives*

As part of the OIG's proactive efforts to promote accountability and integrity and reduce inefficiencies in SBA programs and operations, the OIG reviews changes that SBA is proposing to make to its program directives such as regulations, internal operating procedures, policy notices, and SBA forms that are completed by the public. Frequently, the OIG identifies material weaknesses in these proposals and works with the Agency to implement recommended revisions to promote controls that are more effective and deter waste, fraud, or abuse. During FY 2012, the OIG reviewed 136 proposed revisions of program management or SBA reorganization documents and submitted comments on 79 of these initiatives.

### *Debarment and Administrative Enforcement Actions*

As a complement to the OIG's criminal and civil fraud investigations, the OIG continually promotes the use of suspensions, debarments, and other administrative enforcement actions as a means to protect taxpayer funds from those who have engaged in fraud or otherwise exhibited a lack of business integrity. The OIG regularly identifies individuals and organizations for debarment and other enforcement actions and submits detailed recommendations with supporting evidence to the responsible SBA officials. During FY 2012, the OIG sent 45 suspension and debarment referrals to SBA. Most OIG administrative referrals involve the abuse of SBA's loan and preferential contracting programs. When appropriate, the OIG recommends that the SBA suspend the subject of an ongoing OIG investigation given program risk presented by the continued participation of those individuals and entities.

### *Fraud Awareness Briefings*

The OIG continues to conduct briefings on topics related to fraud in government lending and contracting programs. During FY 2012, the OIG provided 24 fraud awareness presentations for more than 1,100 attendees, including SBA and other Government employees, lending officials, and law enforcement representatives. Topics included types of fraud; fraud indicators and trends; and how to report suspicious activity that may be fraudulent.

## **CONCLUSION**

The SBA OIG continues to focus on the most critical risks facing the SBA. Our resources are directed at key SBA programs and operations, to include financial assistance, government contracting and business development, financial

management and information technology, disaster assistance, Agency management challenges, and security operations. We also will continue to partner with the Agency to ensure that taxpayer and small business interests are protected and served well by reviewing proposed regulations and initiatives, pursuing debarment and administrative enforcement actions, and providing fraud awareness briefings. We value our relationship with this Subcommittee and Committee, and with the Congress at large, and look forward to working together to address identified risks and the most pressing issues facing the SBA.



**Peggy E. Gustafson**  
**Inspector General**  
**U.S. Small Business Administration**

Peggy E. (Peg) Gustafson was sworn in as SBA Inspector General on October 2, 2009. Ms. Gustafson previously served as General Counsel to Senator Claire McCaskill (D-MO), where she advised the Senator on government oversight issues and helped write two bills that have significantly strengthened the federal offices of Inspectors General: the Inspector General Reform Act of 2008 and the legislation that strengthened the office of the Special Inspector General for the Troubled Asset Relief Program.

From 1999-2007 Ms. Gustafson served as General Counsel in the Missouri State Auditor's Office. In that capacity she worked closely with the auditors on issues of the scope of their duties, the auditors' need to access records, and all other legal issues arising in the course of the audits. Ms. Gustafson also served as an assistant prosecuting attorney for Jackson County, Missouri, serving as Chair of the Insurance Fraud Task Force, and as an assistant county counselor for Jackson County.

A native of Chicago, Illinois, she received her B.A. from Grinnell College in Grinnell, Iowa in 1989, and her Juris Doctor from Northwestern University in Chicago in 1992.

Mr. CRENSHAW. Well, thank you very much. Sounds to me like you stay pretty busy. And I guess, you know, what comes to mind when I hear you talk about all that, I wish there was some way that we did not need you as much as we need you. With all the loans that are going out, I mean, when you see all the inefficiencies and outright fraud and corruption, is there anything that you see that could be done on the front end? Why do you think that it is so widespread? Is it just the nature of the beast making loans like this, or the third-party folks that are administering the loans? What are your thoughts on reducing your work and doing a better job on the front end of making sure all this stuff does not happen?

Ms. GUSTAFSON. Well, I think that is a difficult question to this extent: Where there is money, there is always going to be fraud. I am sure that everybody knows that and everybody says that. And so, you know, I think there will always, obviously, be a need for somebody watching the money, be it here, or in Agriculture, or in any department where there is money going out the door. There is going to be somebody out there figuring out a way to take some wrongfully.

So I do not know that it is really possible to do that. I do think, you know, SBA, for an agency of its size, there is a tremendous amount of money at risk in SBA because of the nature of it, because of the guaranteed portions of the loans. The SBA loan portfolio is over \$100 billion right now. The small business contracts, you know, to the extent that SBA has a role, certainly in the 8(a), the HUBZone, that is almost \$100 billion as well. So it is a tremendous amount of money, and on a good day, I am about 100 people. So what I try to do, and I think that the thing that needs to be done is, again, try to proactively, and through my work, identify the risks and see where the process can be tightened. I truly think what all you can do is be forever watchful, make sure that you are notifying the agency and Congress of the things that really need to be fixed to help close these loopholes. You know, every time you close a loophole, they will find another one, so you just have to be vigilant. I really think that that is the best thing that you can do.

Mr. CRENSHAW. You mentioned the lack of resources impacts everybody. We are going through this sequestration, the sequester. We do not know yet what is in the president's request, but we do know that the resolution that the House passed on their budget side and the budget resolution in the Senate, and we anticipate that the sequester kind of stays there, which means it is probably going to be hard to see a lot of increases.

Tell us how it has impacted you. You mentioned you have got one person doing all that. How does it impact not only you, but do you think the SBA as well, and what are you doing to try to deal with that? Because some agencies say, "Well, to some extent it forces us to try to be more efficient." And, you know, there is only so much you could do. But talk about that: (a), how it affects you, and then (b), what you are doing to try to just deal with it.

Ms. GUSTAFSON. Right. Well, as far as my office and the sequester, one important thing to note, and this is very typical of all IG offices, the vast majority of my money, 84 percent of the money that I receive, goes to people. It is salary and expenses. I do not have programs. I do not have stuff. So when you break down my

money, 84 percent is just to keep the people that I have there. Ten percent goes to the financial statement audit, which is a statutorily mandated audit, which is especially important, I think, in the context of SBA because of the amount of money. We have to do it anyway, but, again, because of the credit risks and stuff, that is an important audit. That is about 10 percent of my budget. And 6 percent is everything else, which includes any time my investigators need to travel to Springfield, Missouri, things like that. I mean, that is what it goes to. Training, and when I am talking about training, I mean my auditors need a certain number of CPEs every year, and my investigators need mandated training every year. And that is it.

And so when things like the sequester hit, had I not lost people through attrition or had I filled those jobs, I would be undergoing furloughs right now. I could not avoid it. We have not filled positions as they have come open, and so right now I am down five positions, which, in my office, is pretty substantial, especially because the work that we do takes a lot of time. Audits work in teams, investigators, you know, work in teams. And so when you lose a person, you are really affecting even the efficiency of the people who are there. But I have made that decision so that I did not have to furlough people, which I think is the most unattractive solution. I mean, I would really hate to do that.

What I still may end up doing, given the resources and salary and expenses, I do have some money that I was given under the Recovery Act, that, of course, can only be used when I am looking at recovery, which is fair. And I have also been given money under the Hurricane Sandy supplemental. And, of course, normally what you do, and what we have done and will do in Sandy, is you bring on people specifically to work on Sandy. And I will do that. But I may also have to move some of my resources to that, again, in order to avoid furloughs, which Sandy needs to be looked at, so that is fine. But if I am moving people from my credit programs, for example, then there is a loan audit that is not going on. So it is going to be very problematic for me, but it is the best possible solution, I think.

As far as the agency, you know, I know that the agency has announced they do not have to do, as it stands right now, they did not have to furlough anybody. Widespread furloughs in the agency would be of a concern to me because they are pretty small as they are. I mean, if they start having less people doing the oversight that they do, I would be very concerned about that. So going forward, I do not know what October 2013 holds, but if they start having to furlough, it would be a concern to me about their ability to monitor their programs as well.

Mr. CRENSHAW. You mentioned Sandy. I was going to ask you about the \$5 million that you received to deal with that; how do you go about utilizing those dollars and how do you strike a balance? You have got a hurricane, you have got people in need, time is of essence. How do you balance the desire to get the money to people as quick as you can, but, on the other hand, make sure that you are doing the right processes and avoid some of the things that we are talking about?

Ms. GUSTAFSON. Well, you know, the way that we approach disasters the size of Sandy, the way that we are looking, and I am looking at Sandy, this is the biggest test for SBA since Katrina. And there were certainly many, many well-documented issues and problems with how things that happened during Katrina, and even as it relates to SBA and the deliverables that they were doing. And so one of the things that we will be doing with Sandy is seeing how that worked. I mean, this is really the first test of a wide-scale, multi-billion-dollar disaster. And so we will be going in. And for us, in all honesty, there is not a rush for us to get money out the door, you know, not being the agency. Really, for us, it is to be much more thoughtful and to come in with the plan that we have. And, really, what we do necessarily follows what the agency does anyway. And so I think we do not suffer from some of the same pressures the agency does. This will be like we did with Katrina.

What I anticipate is the first work that we will be doing, we will be doing audit work because the agency is now undergoing the process. They have approved the loans. The money is going to start going out the door. The money goes out later than the loans are approved. And we will be following that with our audits. And then the criminal investigations, which will come, because it is a lot of money, that always follows. You know, that does not happen until later, when the loans start defaulting, or we start hearing the reports of the person in Ohio getting the money, claiming that they had a house in New Jersey. It is going to happen. I do not want to sound like it is too much of a good thing, but we do benefit a little bit in that we do not feel that pressure. And I would not want to do that because I want the money to be used very smartly. You know, I am very grateful. I do not know how we would have overseen \$2 billion as it stands today without that money. But even that, if it is anything like Katrina, and we just wrapped up Katrina, we ended up having two closed cases. We ran out of time and we ran out of money because there is a lot going on. And you run into statute of limitations problems as well. I anticipate Sandy being the same way.

Mr. CRENSHAW. Well, thank you very much. Mr. Serrano.

Mr. SERRANO. Thank you, Mr. Chairman. Mr. Chairman, we are winding down the hearing season. And I just wanted to take this opportunity, on behalf of the folks on this side, to thank you for your style of conducting the hearings and your treatment of us. This sounds like a lovefest here, right? But you are a gentleman and a good guy, and we appreciate that. I certainly do.

Mr. CRENSHAW. Well, there is more work to be done.

Mr. SERRANO. I know. So before it gets heated, I wanted to say something nice.

Mr. CRENSHAW. Your timing is exquisite. I was just getting ready to, no.

Mr. SERRANO. Inspector General, we might as well start with the elephant in the room, and I am not referring to my Republican colleagues: sequestration. And that is, with the effect, what do you know fully the effects so far to be on the SBA, and perhaps, just as important, you know, what is the impact in terms of how it affects small businesses and the community at large. And as people have to adjust to this time we are living in now, some agencies



seem to be able to tell us right away how it affects their ability to deliver services. What can you tell us about SBA in that sense?

Ms. GUSTAFSON. Ranking Member Serrano, at the risk of sounding like I do not know what I am doing, there is very little I can tell you.

Mr. SERRANO. Oh, around here, that is not a strange thing.

Ms. GUSTAFSON. There is very little I can tell you.

Mr. SERRANO. I do it all the time in two languages.

Ms. GUSTAFSON. My perspective comes just from what the agency has said, and I will tell you what I feel, and I think I look at it from a slightly different perspective as, you know, I understand the agencies, which I certainly saw the letter that they sent, saying if there is a reduction in subsidy, less loans will be made. That makes sense. If you do not have subsidies to support loans, you cannot make those loans. So that makes sense to me. I certainly have not gone beyond that to see if there has been a net effect of less loans being made; have not looked at it. Since we are auditors, we would have to actually do an audit to do that.

The other thing that the agency has said is if there are less federal government contracts being let, less small businesses will be getting those contracts. Again, that seems absolutely logical, and I would absolutely anticipate that to be the case. In general, I think a lot of times small businesses get contracts not just because the government, out of the goodness of their heart, wants to give small businesses contracts, but because you have that goal. You have that goal of 23 percent, and the agencies take that goal very, very seriously. And so I think it is logical to think that if the goal is now a smaller pot, they are still going to aim for that 23 percent. And 23 percent now represents a different number. It did represent this before sequestration, and now it represents this. And I think that is what the agencies are going to be aiming for because they do not meet that goal as it is. So they still are going to aim for the goal and probably not meet it. So, again, that makes sense.

Again, what I was most concerned with and what I remain concerned with is if, in the end, there has to be furloughs, depending on where those furloughs are, that is going to concern me because I think they conduct limited oversight themselves to the extent that they can, and so if they are having less people there, it is going to affect their ability to do that. And they are the first line of defense before we are, so that is going to be a problem. I would think it would cause delays. I think it would cause all those things, should it happen. My understanding, from what Administrator Mills has said, is so far it has not.

Mr. SERRANO. So if I was to ask you as an added question what part of the budget is the most vulnerable, in your opinion, I guess it would be the ability to provide the service to meet the goals of 23 percent or other goals that the agency has to meet.

Ms. GUSTAFSON. Actually, I do not know that I could say what is most vulnerable. I think, in general, I certainly think for my office, I am way smaller than I need to be if I were to ever get a handle. For example, to your opening statement, and Chairman to yours, whether fraud is increasing or not, we are so busy, I do not know if it is increasing or not because we are constantly having to turn stuff away, you know what I mean. I do not know that you

ever get to know the universe of fraud, but I know that I know that we have more than we can handle. I think the agency operates a little bit in that same way, which is to say they are as small as they can possibly be without losing effectiveness. I mean, I am sure that there are things that can happen internally. Obviously, there are not things that can be changed, but, again, there is a tremendous amount of money at risk through the programs of the SBA, and so reductions in size would concern me.

Mr. SERRANO. On your point of having to turn things away, I am not understanding that. Does that mean that you have to decide what alleged fraud is more important or bigger than another alleged fraud, or just determining whether it is fraud or not, or both? I am afraid that your statement makes it sound like some folks could get away with something, and that is a concern, obviously.

Ms. GUSTAFSON. That is what I am saying. I am saying that we, at times, have to, I think I have somewhere around the area of 40 investigators, 40 criminal investigators, maybe a couple more than that, and there are times every day they have to make a decision, can I open this case or not? Do I have the resources to open this case, or am I completely full? And that happens all the time. And to your point, the other point happens as well. Again, as I mentioned in my opening statement, we have, for several years, had what we called an early fraud detection working group because there are certain characteristics of a loan that we know to be indicative of fraud. It is a fraud indicator, one of it being whether it defaults very early. Loans that default very early, more likely than other loans, there may have been some fraud in there. Very often, we will do an analysis and say, "Here are the loans that meet enough characteristics it concerns us." More often than not, that is all we can do. We will let the agency know which loans they are, but we cannot do anything further. And I have to say I am sure I am not the only law enforcement agency that does that, but absolutely, it happens.

Mr. SERRANO. Well, we thank you. I had more questions, obviously, but we will wait for the second round. Thank you. And when I said something about the Republicans, I noticed that they got very sad.

Mr. CRENSHAW. They are very engrossed with the president's budget that just got released this morning, so they are, you know, they are preoccupied. Mr. Graves.

Mr. GRAVES. Thank you, Mr. Chairman. Good morning, Inspector General. Just a couple of questions, really in relation to veterans returning and some of the programs that are available to them, and I am sure you are familiar with some. Are there any inter-departmental areas in which they are rating or ranking or scoring the effectiveness of the availability of loans or opportunities for veterans returning from conflict to civilian life and helping them start small businesses? I know there has been some effort from the Small Business Administration.

Ms. GUSTAFSON. I think there has been some effort. I am not intimately familiar. It is a very small part, you know, it is a very small number of people, given the size of the agency. I do know that they have a specific office. I do not know to the extent that they have tried to do ratings or rankings. I do think they try very

much to get the word out and be advocates and things like that, but I do not know that there has been a judge of effectiveness or success.

Mr. GRAVES. So is it just a small part of the SBA's budget that is dedicated to the veterans program?

Ms. GUSTAFSON. That is right. And, of course, there is the service-disabled veteran owned contracting set-aside program as well, which, needless to say, Veterans' Affairs certainly has a role in, too.

Mr. GRAVES. Okay, do you know what percentage that is of the budget that is dedicated to veterans?

Ms. GUSTAFSON. Sorry, I do not.

Mr. GRAVES. Okay. And then on the pilot program, the Operation Boots to Business. Are you familiar with that?

Ms. GUSTAFSON. Very slightly. Not much.

Mr. GRAVES. Okay, okay, because we would like to learn a little bit more about that, and I guess in doing some of the research, it seems like it is very difficult to navigate the websites, a little bit, to discover what is available for veterans, and, particularly, we think that if it is hard for us and our staff in our offices then maybe it is hard for those in our districts as well. So we are trying to get a better understanding of what is available and what is successful. And the Boots to Business program, I know you are not real familiar with it, but we would be interested to know if you think it is being successful as a pilot program. Is it something that should be permanent in the future? And would the department support legislation that potentially did that as well? So maybe you all could get back with us on that.

Ms. GUSTAFSON. Absolutely, Representative Graves. I am happy to get back with that, and we will even contact you and make sure that I have everything that you need. Thank you for asking.

Mr. GRAVES. And then if I could just ask one other, Mr. Chairman. I was listening a little bit about the discussion about the cuts, the sequestration cuts, and some things come to mind, and, on an average, do you know, in the department, how many vacation days an average employee takes a year?

Ms. GUSTAFSON. No, I really do not look at that. I do not know.

Mr. GRAVES. So it would be more than five?

Ms. GUSTAFSON. Oh, I could not even begin to speak to the agency. I mean, I know they are all career employees, so they get a certain number of days. I know that we have not had a complaint about it, but does not mean it does not happen.

Mr. GRAVES. Right. So to help me, how many vacation days do you get a year?

Ms. GUSTAFSON. Well, I do not get any. As a presidential appointee, actually, I do not get any.

Mr. GRAVES. You do not get any. Okay. But a non-appointee?

Ms. GUSTAFSON. It depends on level of service. I am actually not in the career. I am not a career. But I know it depends on years of service, and it increases depending on years of service. I would assume, this is a big assumption because their Human Capital Office is a work in progress, but I would assume that that is something that is probably available in a quick spreadsheet or something for you that, again, I would be happy to ask. Okay. I have received a note from the field. If you have been a government em-

ployee for less than three years, you get four hours per pay period; three to 15 years, six hours per pay period; and 15 years, eight hours per pay period. And I do know there are limits on how much you can carry over.

Mr. GRAVES. Pretty quick notes there, yeah.

Ms. GUSTAFSON. I have career people behind me, they know. I just do not know.

Mr. GRAVES. And with that, there are sick days, I guess, as well.

Ms. GUSTAFSON. Right, right.

Mr. GRAVES. And so I would be curious what your definition of furlough is because we hear furlough referred to quite a bit, and it is, you know, a negative connotation.

Ms. GUSTAFSON. My definition of furlough is that you are taking a day where you do not get any pay.

Mr. GRAVES. Right.

Ms. GUSTAFSON. A furlough, where, with notice, you know that for every pay period, for example, there is one day that you are not working and not getting paid for. That is my definition of furlough.

Mr. GRAVES. And in your description of the impact of furloughs, it was more of, they would not be able to provide as many services or loans to those who are seeking them. But then I tried to correlate that with, well, employees take days off for vacation, or they take them off for a sick day, and it does not seem to slow the process down. So I do not see where you draw the connection that a furlough day, while I do agree with you that it is a day without pay that someone is not working, I do not know how that impacts the work delivery if vacation does not impact work delivery or sick days do not.

Ms. GUSTAFSON. I think not being at work impacts work delivery. I think that if you are going to furlough somebody they are probably going to be at work even less, do you know what I mean? I mean, you know, I guess that I would anticipate this as an add; you know, I think that employees would take their vacation and they will take their sick, and there will be one day where they are not paid. So I guess it was just as if more people were taking sick or they were taking more sick or vacation days, I just envision less people at work. So, and, you know, assuming everybody is working when they are at work, and the longer it goes, I would assume that there is going to be some impact on it.

Mr. GRAVES. But the longer an employee is with the agency, the more days that they are granted to take off, so the logic would lead me to believe, that if you are having difficulty delivering services, then why do you encourage more people to take more days off the longer you serve, but taking one off to save the republic is a different question.

Ms. GUSTAFSON. Right, well, you know, I guess I just think that if one day every two weeks the SBA is closed, I think that is going to have an impact on timing, on efficiency; I think that that is going to happen.

Mr. GRAVES. Not closed; it is going to be rolling furloughs.

Ms. GUSTAFSON. Right.

Mr. GRAVES. The state of Georgia has been through a tremendous amount of furloughs over the last several years; teachers have been furloughed 10, 11, 12 days, but voluntarily saying, you know

what? I am willing to do that for the state because, one, I know it is important; number two, I know that I get to keep my job, but I am being a part of the solution. But here on the federal government level, it just does not seem to be as accepting. Mr. Chairman, I think my time has been expired. Thank you.

Ms. GUSTAFSON. Thank you.

Mr. CRENSHAW. All I know is when you read how you determine holidays or days off, you have got to get an accountant to figure out the pay period times, the hour times, whatever.

Ms. GUSTAFSON. I know, they know it. Believe me, I think the employees know, Chairman, I just do not.

Mr. CRENSHAW. I think you just muddled it so he would not understand, but you did a good job. Mr. Yoder.

Mr. YODER. Thank you, Mr. Chairman, Mr. Serrano. Peggy, thanks for being here today. You did not turn me off there, Mr. Serrano, did you? I noted that you had worked for Senator McCaskill; as a Kansan, we appreciate having Missouri nearby, but it does not make you a Missouri Tiger fan, though, does it?

Ms. GUSTAFSON. I lived in Columbia for eight years, so, yes.

Mr. YODER. Did you catch the cold there of being a Missouri Tiger fan?

Ms. GUSTAFSON. Well, I noted you were from Kansas.

Mr. YODER. Okay, so we will just agree to disagree on that. I noted your testimony in some specific areas, and one of the issues that you raised is the exposure that has been discussed already a little bit today, the exposure that the SBA has with loan guarantees; that is a big part of what the SBA does. Do you have thoughts on what the right balance is? I know you noted that there is a statutory change in 2010 that increased the size of the loans that SBA should be able to guarantee, and that creates additional exposure. Do you have thoughts on what that right balance is between exposure to taxpayers and providing assistance maybe that the private sector lending is not able to support? How necessary is that? Should it grow? Should it shrink? What is that sweet spot?

Ms. GUSTAFSON. I tend to leave the policy questions of whether it needs to be \$2 million and whether it needs to be \$5 million to the policymakers, which I am most certainly am not, so I do not. Really, the nature of my work and my focus is always, are we, and as SBA, doing the best job given the fact that there will be more exposure, given that the fact that these are bigger loans. And if a \$5 million loan defaults, it is a couple million dollars more than a \$2 million, and that is just more money for the taxpayers. And so, really, my focus is just, is the oversight of this lending as strong as it needs to be to protect the taxpayers, whether it be \$2 million, whether it be \$50,000 express loan, which, often, they default pretty often, too, so that is really what my focus is, so I do not have an opinion on a sweet spot.

Mr. YODER. And you discuss in your testimony that we need to strengthen oversight, that the standards need to be modified; can you discuss, on those suggestions, things that we might be able to implement in terms of policies, that when we have the SBA before us, we might suggest on what we are doing with our budget changes that we could specifically could make? I mean, certainly, we can raise these suggestions you have made as concerns. Are

there thoughts in terms of what Congress could do to tighten up? I know, again, it is back to a policy question.

Ms. GUSTAFSON. Right.

Mr. YODER. But based upon your findings, what could fix some of those problems on our end?

Ms. GUSTAFSON. I very much appreciate your question because I think the best reference for you, and something that I am happy to talk about right now, would be our management challenges report which comes out once a year because there are several challenges that have existed a long time that deal with lender oversight and talk about some things, that it is not even a policy change; often, the best thing that you could do for me is just ask them about it because they do listen to me but they do not have to listen to me, and they do not have to do what I think they should. But they listen to you, and kind of have to do what you think they should do, so there are certain things, I mean, they have gotten better at lender oversight.

What I have personally seen in my three years there is they are taking a more risk-based approach to their lender oversight, which I think is key. I mean, I think they need to be smart about how they are choosing to look at the lenders and what they are doing. You know, I think it just makes for better oversight, and I think that the lenders appreciate that more, too. I mean, rather than just doing a one-size-fits-all, we are going to do a quick annual review of everybody and do a check-the-box, what I have seen through the Office of Credit Risk Management, OCRM, as they have new head since I have been there, a man named Brent Ciurlino, I should not say that name, they will probably treat him badly now, but is they are being smarter where do we need to focus when we are doing our lender oversight, and I think that that is really important and it needs to be appreciated that they are doing that. They brought Mr. Ciurlino on; I think that was a big step. I think the agency needs to be encouraged to give OCRM all the support that it wants and needs because I think that they are heading in the right direction as far as lender oversight.

We have some concerns about the improper payments in 7(a) program. There is some concerns about their quality assurance reviews that we are still working through; again, that is part of the management challenges. I think that it would be helpful to talk to them about that, because, again, I think that they are getting there but I think it would be helpful to hear about that.

Mr. YODER. And just finally, Mr. Chairman, certainly, I think in our debates in Washington, D.C., we focus a lot on the economy, job creation, unemployment. We know from reams of data that the majority of the jobs that are going to be created in a post-recession environment, almost 100 percent of the jobs are going to come from small businesses, new companies, start-ups, innovators, entrepreneurs, those types of folks in our country. And so as you review the SBA, and giving it, hopefully, the most extensive review that it gets in this process, are there ways that we can make the SBA, again, another policy question, more effective at reaching more of these start-up companies in particular, helping new companies get off the ground? And certainly the SBA plays a role; but, I mean, how many companies is the SBA touching? Would it be important

to increase it as such, is the SBA a value in that process and how could they increase their value to taxpayers? My guess is that most of our small businesses do not have a lot of interaction with the SBA to get it off the ground. We know that new corporate formations is at a 20-year low in this country, and so I think a lot of us are concerned with, okay, we are not starting new small businesses at the same rate we need to. They are not growing, folks are not taking risks, they are not expanding, and so we talk about what we can do here in Washington, and as it relates to this, you know, SBA, what a perfect place to address those concerns.

Ms. GUSTAFSON. I do think, kind of as you intimated, that is a much better question for the administrator in that it is a policy question, but I do have a couple thoughts on that. One is, it does seem to me from what they have stated that SBA consider that to be one of their very important jobs. Now, one of the things that has been noted in a couple reports, specifically in the GAO reports, is, I think there is some question about, kind of, the counseling centers. One of the main ways that citizens do have contact with SBA or other government agencies are through several, several different types of counseling centers located throughout the country. SCORE, which is the retired executives, there are women's counseling centers, there are veterans counseling centers.

And one of the questions that I think might be helpful to have the SBA think through, and is something that has been raised in these GAO reports, is whether those centers are duplicative, whether, perhaps, some of these resources might be better used if there is a consolidation of them. Commerce has some of these centers. Agriculture has some of these centers. SBA has some of these centers. I am not saying absolutely they need to be eliminated or gut down to one, but I think there are questions there about efficiencies in that, such that I think if the agencies, and, again, the GAO duplicative report, the first one that they issued, which was at least a year ago pursuant to statute, talked about these centers. It raises, I think, a lot of good questions, especially in these times that I think should be thought through about whether the federal government is doing this as smartly as they need to, because it has become, just like in many times in the lending programs, because there are lending programs in several different agencies, it is a patchwork, just kind of in the nature of the government. And maybe it is time to take a look at that and see if there can be more bang for the buck by kind of combing through that and doing it the most efficient way possible.

Mr. YODER. Great. And thank you, Inspector. Thank you, Mr. Chairman.

Mr. CRENSHAW. Thank you. Ms. Herrera Beutler.

Ms. HERRERA BEUTLER. Thank you. And I am not sure I am going to have the right name of this program. So this might be a follow up conversation, but it is something I am very interested in.

In recent weeks I have had some small mills in my area contact me, timber mills, regarding a program through the SBA where it is incentivizing timber sales. And what they are expressing to me is some real challenges, that the SBA is not, and I am trying to get details on it, but not fulfilling, basically, I do not know if it is

the letter of the law or the spirit of the law with regard to the set-aside. Are you familiar with it?

Ms. GUSTAFSON. I am not but, you know, we can go back, and we can get more information.

Ms. HERRERA BEUTLER. I would very much like to.

Ms. GUSTAFSON. I can make sure that the agency knows that they are asking us, and they will know, and we can get you some answers.

Ms. HERRERA BEUTLER. That would be great. I will get you all the specific information. I was just hoping you would know. It is like my memory, I am going two months back in my calendar going, okay, I had the title of this program, and I do not remember it. But I believe it is the only, within SBA, I believe it is the only program that deals with timber sales for small mills.

Ms. GUSTAFSON. Sure.

Ms. HERRERA BEUTLER. So I do not think there are a lot of them.

Ms. GUSTAFSON. Right, one would think. But, yeah, but we can definitely look at it. And I am sure, in the big scheme of SBA, it is small enough such that we may not have looked at it, but it does not mean that we cannot get you answers. We can do that.

Ms. HERRERA BEUTLER. That would be great. That is what we would like to follow up on. So that is it.

Ms. GUSTAFSON. All right.

Ms. HERRERA BEUTLER. Thank you, Mr. Chairman.

Mr. YODER. Thank you. Mr. Quigley.

Mr. QUIGLEY. Thank you, Mr. Chairman. Morning.

Ms. GUSTAFSON. Good morning.

Mr. QUIGLEY. Earlier in your testimony you talked about your staff having to make decisions about whether or not to pursue a case. What number of people are we roughly talking about?

Ms. GUSTAFSON. On that I was talking about my criminal investigators.

Mr. QUIGLEY. Right.

Ms. GUSTAFSON. Right. And I think that I am at, I should know that off the top of my head, I am either at 40 or 42. About 40, 40. And I am about 100, as far as my professional staff, I am almost evenly divided. I have more criminal investigators than auditors right now, but we are talking about 40.

Mr. QUIGLEY. So when you talk to them or their supervisors, this choice you talk about them having to make. Do you talk in general about how to set that criteria, I mean, besides a judgment call? Is it likelihood of winning? The amount in question? Who the victim is? How egregious this is? I mean, what are the criteria, or do you let them decide that for themselves?

Ms. GUSTAFSON. They are not on their own just deciding for themselves. First off, I will tell you that we are talking about a universe of cases. I can even limit this conversation to likelihood to win. You know, we are talking about cases where we think that there is a potential to win. Very often that decision is made certainly with supervisors, but also, quite frankly, my criminal investigators work very closely with their U.S. attorneys and their assistant U.S. attorneys wherever the crime is located because, often, one of the factors has to be will the prosecutor, at least to go crimi-



nal, will the prosecutor take this case. Or if they are not going to take this case, they also say, will the civil attorney take this case.

Mr. QUIGLEY. Prosecutors like to win their cases.

Ms. GUSTAFSON. And they like to win big cases. So it is never, you know, it is not a function of us bringing cases that they are not going to win, it is a function of bringing cases that they are going to win big.

We have a loan case made by one of my agents in D.C. that involves \$100 million loss to the SBA, \$100 million. We have a case, again, involving contracting, and bribery, and kickbacks involving, I think it was, a \$1.2 billion contract and they were trying to steer an almost \$780 million contract, and there were, we proved, at least \$20 million in kickbacks. Not every case I have is a \$20 million or \$100 million case, but they are big, they are really big.

Mr. QUIGLEY. But we do not want to give people the impression in this country that if you steal \$10,000 or \$20,000, no one is going to come get you. So how do we avoid that perception? How do you at least go after enough of them to scare people to think that, well, the decimal point is in the wrong spot for them to come after me.

Ms. GUSTAFSON. Well, one of the things that I am actually most proud of my office recently is we have had some really big victories, and when I say big victories, I mean to the community who is caring about this stuff on just those type of cases. So, for example, you know, we have the HUBZone program which involves contracts which tend to be smaller and which involve cases that tend to be more complex. And I will tell you that I think, historically, sometimes those cases are hard to get accepted because a prosecutor also likes a case that is easy to win because it saves them time. And the HUBZone program is very complicated. There are all these, you know, you have to have so many people that live in the HUBZone. And you have to attempt to maintain that residency and all of that. But we had a very big victory in Kentucky in a HUBZone case that resulted in a multi-million-dollar judgment. Now, I will tell you that when we get those type of cases, we just had somebody plead guilty to a case where he had not even gotten a contract, but he had lied to get into the 8(a) program.

Now, those cases, I think, have a very chilling affect because I think the people who matter are paying attention to those cases. And so I have been very heartened because it seems like there is definitely an appetite for those cases on the part of many of the prosecutors. They often tend to be U.S. attorneys because they are federal cases. It is federal statutes.

But I think that especially in the contracting arena, which has been traditionally harder to do because you have a contract where the government is getting what they were supposed to get. And so sometimes prosecutors used to be, well, you know, okay, so maybe he should not have gotten the contract, but at least you got your widgets. I am seeing a turn in that, and I am seeing that there is an appetite for those cases, which is great, because, personally, as a former prosecutor, I think they have tremendous jury appeal because that really upsets citizens who are playing by the rules, you know. And I think we have had some really good victories. And, like I said, I think that the people paying attention to that, the

loan cases, the contract cases, they are being noticed. So I do think that that message is getting out.

Mr. QUIGLEY. I think there is some inside sports involved to the point you made that people who work in this field follow that stuff.

Ms. GUSTAFSON. Right.

Mr. QUIGLEY. But I am curious if there is another way to let people out there who would play games with this. I mean, how do you publicize these cases? I mean, how does it get out to the general public?

Ms. GUSTAFSON. Well, very often, DOJ takes the lead on that, which is fine, which is fair. They are the attorneys. So they do get out. But I do think, and, again, it might be insider baseball, but I do note that on all the papers that we all in this room tend to read, the GovExecs, those things, The Federal Times, things like that, The Fed Page on the Washington Post, again, that is insider baseball, but these cases will get noticed in that.

A lot of times in the lending community, some of my biggest cases, the one in Baltimore and then also I have a very large case in Missouri, actually involves, like, a community, I mean, people who kind of know one another, and it just kind of gets out. This was in Springfield, Missouri.

Mr. QUIGLEY. And I appreciate that. I guess my final point would be, and we talked to the administrator, perhaps, but you could encourage this as well, through the application process reminding people of what prosecution can mean to them would help as well.

Ms. GUSTAFSON. And to your point, and I appreciate you making that point, one of the conversations that I have actually been having is, is I think that the SBA website is a tremendous place to put that kind of notice. And I think you are right. I think you could reach a lot of people that way. I think some of these cases that I am talking to you about now that I guess I would call smaller, and, to be fair, maybe that is not giving them enough credit, I think that there are ways to publicize that, and that will reach a lot of people. So I appreciate your thoughts on that.

And I would say that mentioning that to an administrator would only help as we go forward because they certainly do those portals that the public often visits. You know, we have a presence on the web, but we are way on the bottom on this side. That is where they put us.

Mr. QUIGLEY. Well, I appreciate that, and I thank you for your service.

Ms. GUSTAFSON. Thank you.

Mr. QUIGLEY. Thank you, Mr. Chairman.

Mr. CRENSHAW. Thank you, Mr. Quigley. We have got time for a couple more questions. And one thing that keeps bothering me is to hear you talk about is that there is an awful lot of money involved, and so it is almost like we just assume there is going to be a lot of fraud, a lot of corruption. And then, of course, you got to come in at the end and try to catch everybody. But if we got \$100 billion out, part of those loans are made by outside kind of third-party lenders. And Mr. Yoder talked a little bit about it. Somehow we got to do a better job of having oversight on these lenders. Maybe it is a point well taken that we ought to talk to the

SBA and say, "How do you decide who is going to oversee these loans?"

Then the other part is you got these improper payments. And once again, it is just like you assume we got \$800 million that is going to go for hurricane relief, and we just sit here and assume a lot of that is going to get wasted. People in Ohio are going to ask for money. And somehow, again, that is not your problem. That is a policy decision that SBA has got to do a better job of. But maybe you get to see that; you see it up close, you tell them they are making improper payments. I think I read somewhere they said, "Well, we are not making any improper payments." You said, "Well, you made like 1,100 improper payments."

Ms. GUSTAFSON. Right.

Mr. CRENSHAW. I think in the 7(a) it is like 20 percent; Disaster it is 17 or 18 percent.

Ms. GUSTAFSON. Right.

Mr. CRENSHAW. So from your perspective, and when we talk to them, we are going to encourage them to do a better job, but in your view, is that just lack of oversight, or is it outright fraud, or is it a combination of both? I mean, how are we going to solve the problem so that you do not have to clean up such a big mess every time?

Ms. GUSTAFSON. I think that there are a couple of things. I do think that historically, and I am going back truly historically, SBA really viewed itself solely as an advocacy organization. I mean, I really think that they took very seriously and fairly, that their job was to make sure that the money was going out the door and serving the public because that is why they were there. I think that their focus on oversight is often very, very, very secondary to that. And I think the fact that they view themselves as an advocacy organization kind of cuts against them seeing themselves as an oversight organization because sometimes they get worried, well, we do not want lenders to leave the program. And, of course, you do not want good lenders to leave the program. I would argue maybe not so much if there are bad lenders, it would not be the end of the world if they left the program.

So I do think that they need to constantly let it be known that they do have a role in oversight. And you are right, the fact that the lending authority is now delegated caused a sea change. It is vastly different from what it was when SBA was created, and they were all direct loans.

Again, as I said earlier, I personally, and again, I have three years there, have seen them spend more time and talk a lot more about their role in oversight, and their role both in lending oversight and in contracting oversight which is a key first step, because the message has to come from the top, especially one that had not been the message before.

Mr. CRENSHAW. It sounds like it is almost like they view it as a grant program. That is a point well taken. We want to help everybody. We want to get the money out.

Ms. GUSTAFSON. Right.

Mr. CRENSHAW. And somebody said, "Wait a minute. I think they are supposed to pay this back." And so now we are kind of focusing on making a good loan that has a chance of being repaid.

Ms. GUSTAFSON. Right. Right. And to be fair, obviously, you know, I would hate to come out of this thinking that I thought that lenders were doing a bad job. I mean, I think the lenders take their job very seriously, and I mean, they are banks. I mean, they take their responsibilities very seriously, and they do not want to make bad loans. And so I do not want to imply that all heck is breaking loose because, you know, they have guarantees. I mean, I certainly would not go that far. But I think that you are right. I do think the focus on improper payments is one that I, personally, have had very animated disagreements with the administrator on this because I do not know if they take it as seriously as they should.

You know, I was actually on the Hill when the Improper Payments Act, I worked with people on this and Homeland Security, and so I know how important it is. And, you know, I do not think it is enough to say, well, the loan is getting repaid, so it is going to be okay. Or, you know, they did the best they could. I do not think that that is what the Improper Payments Act means. And I struggle with them. I struggle sometimes because I do not think the agency necessarily always sees it that way.

Now, I think the agency will tell you that they are making progress, and, you know, the Improper Payments Recovery Act is just a couple years old. And our annual review has shown that they are getting better in their processes. But, you know, I have unfortunately also seen when I first came, kind of, they were here on 7(a), and I was here. We kind of came closer together. Well, I should not do it that way. They moved closer to me. As we went through, their rate actually came much closer to mine. And the next year I found myself in the exact same position, where I was up here and they were down there, and that was frustrating for me.

You know, I think there is, you know, a fear of the improper payments rate such that, you know, that they are disagreeing with me. And, I mean, I think my rates are right. And you are right; my last 7(a) rate was still substantially higher than theirs. We did not go behind theirs. And so I think that focusing on that and emphasizing that that is something that is very important would be extraordinarily helpful.

Mr. CRENSHAW. I think that would be a thing that we could help as we talk to those folks.

Ms. GUSTAFSON. Yeah.

Mr. CRENSHAW. And just in terms of recovery.

Ms. GUSTAFSON. Right.

Mr. CRENSHAW. I understand that they do not seem to have that as a priority. You make a bad loan; it does not get paid back. I think what I hear you saying is sometimes you are charged with finding the things that go wrong.

Ms. GUSTAFSON. Right.

Mr. CRENSHAW. And what might look like fraud, it might look like administrative lack of oversight, somehow we need to encourage the agency to just do a better job. It would just save us all a whole lot of money, the taxpayers, the government, everybody else, if they did a better job. Actually, then we would not have to give you as much money to go out and catch all the bad guys.

Ms. GUSTAFSON. It certainly costs less to stop the money going out the door than to go back and get it. But to your point, our last Improper Payments Review noted that one of the things in the Act that they have not yet shown is they are supposed to do a cost benefit analysis about whether recovery audits would be feasible and worth the time. And that had not been done by the time of our Improper Payments Review. I think they said it would be done by the time they released their annual financial report to the president, I think it was.

But I would strongly encourage you to, when they do make that decision, ask them how they decided. Because if I were a betting girl, I would bet they are going to say it is not worth it.

Mr. CRENSHAW. Well, we appreciate that. Mr. Serrano.

Mr. SERRANO. Thank you. You know at the expense of sounding like I am going to praise you all day, that was masterful how you went around, around, around, to come to your important point of, therefore, we can give you less money in the future.

Mr. CRENSHAW. It just happened.

Mr. SERRANO. That is good work. Somehow I would have come up with a different. You need to grow. We call it investment.

Ms. GUSTAFSON. Fivefold return.

Mr. SERRANO. Yeah. You know, you are so right, Mr. Chairman, for so many years. And I have been doing this for a long time now. There are a lot of people out there who actually think that SBA is strictly a grants program, that somehow there is no repayment involved. And when we tell them there is, they go, "Really?" And we say, yes. It is like the rest of us, so, but, you are right. Some things we have to work on.

You know, one of the things that we learn when a tragedy hits home is what other people go through. Once Congress dealt with the Katrina issue, to many of us, unfortunately, that was out of sight, out of mind, it is over.

Ms. GUSTAFSON. Right.

Mr. SERRANO. And now that we are dealing with the affects of Hurricane Sandy in New York, we know that these are things that will last for a long, long time. The September 11 attacks these many years later are still very much a health issue, a business issue, an emotional issue in New York, a security issue in New York.

So what have you learned, in your opinion? What has the SBA learned from dealing with Hurricane Katrina that they can now apply to dealing with Hurricane Sandy? Because as this continues to be an issue, of course, there is, you know, everything, from, "When are the loans coming? When are the dollars coming?" It is always a matter of, you know, the red tape, and paperwork, and so on. There are other related issues that have to deal with mold removals and the whole thing. But what do you think we learned from Katrina that we can apply to Sandy and to further situations, because, unfortunately, you know, it is not made up by the media, this weather situation seems to be getting rougher and rougher all the time.

Ms. GUSTAFSON. Well, I think, you know, I would like to kind of defer my answer. I will know better how well they learned when we get in there and do some audits to see how well they did com-

pared to Katrina, you know, some of the lessons learned. I do think one of the key lessons from Katrina, certainly both for the IGs and for the agencies is, you know, it is almost fantasizing to me, one of the most interesting things about a natural disaster is how many different federal agencies have a crucial role in that disaster and how disparate those agencies are, up to and including the SBA. I mean, I would think the average homeowner does not think, if my home is destroyed by a hurricane, the Small Business Administration is where I am going to get the loan. I mean, the word "business" is in there. I mean, who thinks that that is where you get the loan to rebuild your house?

So, I think one of the key lessons for Katrina is going to be if the coordination has worked better as far as how the federal government responds to a disaster. And again, and I am not talking about the bottles of water and stuff like that, but I am talking about the aid to the victims. And I think that we certainly saw some big issues with that. We saw a lot of duplication of benefits because FEMA gives money, SBA loans money, and HUD, later, through Community Development Block grants in the states gives money again. And sometimes the money is for the same thing, and, you know, there is supposed to be a certain priority for the money, and, quite frankly, the way the system works is to the extent that you can pay it back, the government wants that money back. I mean, priority is supposed to be given to the loans. But what we saw in Katrina that is concerning to me, especially in these economic times, is a lot of times through the Block Grants that came later, they were used to pay off the loans, so that the government was paying itself back, and then the people got grants for that purpose.

And our audit in that, I forget how many hundreds of millions of dollars that we found that we thought were duplication of benefits, and it was because HUD comes in later, and there can be confusion over who is supposed to do the priorities and in what order, and what that money is supposed to be used for. Homeland Security has a key role in prioritizing it, but one of the difficulties is, to be fair, they are also focused on their mission. I mean, HUD has a very specific mission; FEMA has a very specific mission on dealing with the victims; SBA has their own mission. I think sometimes that gets lost, and, for me, especially because of the money issue, that is going to be something that is key for us to see if that has improved because I think that could be significant money.

Mr. SERRANO. Right. Well, I know that you will stay on top of it, and in the process to make sure that this happens and the money flows. I have one last question, and it is, in your testimony you highlight several areas where the SBA made improvements based on your recommendations. You know, Inspector Generals are seen sometimes as, you know, being in the way. What is, in general, your relationship to the SBA, and then if it is not perfect, you know, what needs to improve, in your opinion?

Ms. GUSTAFSON. If it is perfect, I am probably being too nice, to be fair. I mean, I think that that is true.

Mr. CRENSHAW. By the way, after they get the transcript of this hearing—

Ms. GUSTAFSON. I do not know if they are here right now, so I guess it depends—

Mr. SERRANO. You mean this is a public meeting?

Ms. GUSTAFSON. You know, I spent eight years in an auditor's office before I came to D.C., and we were always viewed as the enemy, and we were always viewed as, "You only come here and tell us what we are doing wrong," which was our job; "Why can't you ever tell us what we are doing right?" Well, that is your job, do it right. But, you know, I do think that it is important, and what I have strived to do is to have a respectful relationship with the agency. And I think, you know, I do want to be fair on that. Improvements have been made. On improper payments, they have made improvements in the reporting. The quality assurance, for example, in the 7(a) program on improper payments is a concern, but in the management challenges, we made clear that at least they have one; I mean, it truly is progress, I am not trying to belittle that. I mean, they are making progress, and I tried to make those points to the extent that I can without all of the sudden having a 600-page report to tell them everything they did right in the last six months.

So I think in that way it is a good relationship. I think in other ways it is a typical relationship; you know, they hate to see us coming. I mean, you know, that is every agency, they just hate to see the IG coming. But it is working. I was heartened in the management challenges that we had, I think, six go up, six made progress. And I think that that is very good, and I think that that was more progress than historically often happens. And so I think that that is good, and I hope that that message comes out, if not here in the transcript, at least in the report.

Mr. SERRANO. Right, sounds something like Congress' relationship with the media. We have been waiting for that one story that says that we have done a great session and did everything right. Yeah, I am not going to hold my breath. Anyway, thank you so much for your service. Thank you for your work. Please, please keep an eye on the whole Sandy thing.

Ms. GUSTAFSON. Yes, yes.

Mr. SERRANO. Like I said, it is something we did not know existed, and we saw it upfront, and it is very sad.

Ms. GUSTAFSON. Right.

Mr. SERRANO. And I think we need a lot of help. Thank you so much.

Mr. CRENSHAW. Does anybody else have any questions? Well, once again, we thank you for spending the morning with us, appreciate the work that you are doing very, very much.

Ms. GUSTAFSON. Thank you. Thank you very much. Thank you, Chairman.

Mr. CRENSHAW. Thank you. This meeting is adjourned.

**Financial Services and General Government Subcommittee**  
**Hearing on the Small Business Administration Office of the Inspector**  
**General**

**Questions for the Record Submitted by Congressman Tom Graves**

***Sequestration: Effect on Making SBA Pilot Programs for Veterans Permanent***

As you know, the SBA has a number of pilot programs and loan programs to assist veterans.

Question: What percentage of the SBA budget is designated to assist veterans in entrepreneurial training for small business start-ups?

**The U.S. Small Business Administration's (SBA) released its *FY 2014 Congressional Budget Justification and FY 2012 Annual Performance Report* (FY 2014 CBJ) contemporaneously with the *The President's Budget for Fiscal Year 2014*. Table 10 of SBA's CBJ indicates that the President is requesting \$18.624 million for Veterans Programs within SBA, which includes Veteran's Business Development and National Veterans Entrepreneurial Training activities.**

Question: Are you aware of inter-departmental offices that rate and promote programs that are found to be successful?

**The Office of Inspector General (OIG) is not aware of inter-departmental offices that rate and promote the Administration's programs.**

**The OIG's mission is to provide independent, objective oversight to improve the integrity, accountability, and performance of the SBA and its programs for the benefit of the American people.**

My staff has had a difficult time navigating your site and the other government sites that have programs available to help returning veterans start small businesses and I have concern that many of the veterans in my district may have similar difficulties as they are attempting to obtain start-up loans in establishing a small business.

Question: If the SBA is forced to furlough employees and make drastic budget cuts as a result of the sequester, which office would be tasked with consolidating the programs and making the information more readily available for veterans?

**Management of the SBA website is under the purview of SBA program officials.**

**Similarly, management of this program is under the purview of SBA program officials. The SBA Office of Congressional and Public Affairs is best positioned to provide responsive data.**



Question: At a time when your agency is facing massive budget cuts due to the Sequester, how are you able to assist with this task?

**Management of this program is under the purview of SBA program officials. The SBA Office of Congressional and Public Affairs is best positioned to provide responsive data.**

***SBA Pilot Program: Operation Boots to Business***

As you know, with an increasing number of returning veterans who leave the service and are transitioning to civilian lifestyles, there are thousands who will be entering the civilian workforce with a very specialized skill-set. My staff has briefed me on SBA's pilot program Operation Boots to Business.

Question: How successful has this program been in its pilot stage?

**The OIG has not independently reviewed Operation Boots to Business. The SBA FY 2014 CBJ indicates the following:**

**The FY 2014 budget includes \$7 million for Boots to Business: From Service to Start-Up, which is designed to expose the more than 250,000 service members returning each year to the opportunities of small business ownership and entrepreneurship. The initial rollout of the pilot is being implemented by the Marines. The goal is to provide training and counseling services for approximately 20,000 returning Marines in four pilot locations: Quantico, Virginia; Cherry Point, North Carolina; Camp Pendleton, California; and Twenty-Nine Palms, California. Following the assessment of the pilot, Boots to Business will roll out nationally to all branches of the military in FY 2014.<sup>1</sup>**

**The SBA Office of Congressional and Public Affairs is best positioned to provide responsive data pertaining to the referenced pilot assessment to be conducted by SBA program officials.**

Question: Where does the funding come from for this project?

**Management of this program is under the purview of SBA program officials. The SBA Office of Congressional and Public Affairs is best positioned to provide responsive data.**

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<sup>1</sup> U.S. Small Business Administration's FY 2014 Congressional Budget Justification and FY 2012 Annual Performance Report, page 6,

Question: How much money has been spent on the pilot program?

**Management of this program is under the purview of SBA program officials. The SBA Office of Congressional and Public Affairs is best positioned to provide responsive data.**

Question: Is there a tax relief component of this program, or is it strictly focused on job training?

**Management of this program is under the purview of SBA program officials. The SBA Office of Congressional and Public Affairs is best positioned to provide responsive data.**

Question: What obstacles have you run into thus far, if any?

**Management of this program is under the purview of SBA program officials. The SBA Office of Congressional and Public Affairs is best positioned to provide responsive data.**

Question: How many veterans have utilized this program thus far and what are the numbers of those who have opened businesses as a result of going through this training program?

**Management of this program is under the purview of SBA program officials. The SBA Office of Congressional and Public Affairs is best positioned to provide responsive data.**

Question: Do you see room/a benefit for this program to be expanded?

**Management of this program is under the purview of SBA program officials. The SBA Office of Congressional and Public Affairs is best positioned to provide responsive data.**

Question: What other programs have been successful and would you recommend making them permanent as well?

**Management of this program is under the purview of SBA program officials. The SBA Office of Congressional and Public Affairs is best positioned to provide responsive data.**

WITNESSES

	Page
Gustafson, Peggy .....	193
Hoecker, C. W .....	1
Tangherlini, D. M .....	127
White, M. J .....	45

